PUBLIC VERSION

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Library of Congress
Washington, D.C.

In the Matter of:	Docket No. 16–CRB–0001–SR/PSSR (2018–2022)
Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)	

MUSIC CHOICE'S WRITTEN REBUTTAL STATEMENT

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WRITTEN REBUTTAL TESTIMONY OF DAVID J. DEL BECCARO

WRITTEN REBUTTAL TESTIMONY OF DAMON WILLIAMS

WRITTEN REBUTTAL TESTIMONY OF GREGORY S. CRAWFORD, PhD

EXHIBITS

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MUSIC CHOICE'S WRITTEN REBUTTAL STATEMENT

Pursuant to 37 C.F.R. § 351.11 and the Judges' Notice of Participants, Commencement of Voluntary Negotiation Period, and Case Scheduling Order dated March 14, 2016 and the Judges' Order for Further Proceedings and Case Scheduling dated June 28, 2016 (the "Judges' Orders"), Music Choice respectfully submits this Written Rebuttal Statement.

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VOLUME I: WITNESS TESTIMONY

Pursuant to 37 C.F.R. § 351.11 and the Judges' Orders, Music Choice submits written rebuttal testimony from the following expert and fact witnesses, included in Volume I:

(1) David J. Del Beccaro, the President and Chief Executive Officer of Music Choice, presents further testimony concerning the business operations of Music Choice and the propriety and effect of the rate increase and regulatory changes

proposed by SoundExchange and various other recording industry entities in this proceeding (collectively, "SoundExchange"). First, Mr. Del Beccaro explains why SoundExchange's only benchmark—the rates currently applicable to "new" (*i.e.*, not "pre-existing") subscription services offered through residential cable and satellite television providers (the "CABSAT" services)—is unreliable and does not reflect market rates, including because it is solely the product of a settlement agreement that expressly prohibits SoundExchange from attempting to rely upon the CABSAT rates and terms as a benchmark in this proceeding. Mr. Del Beccaro further testifies that this settlement agreement is neither a reliable benchmark nor indicative of any fair market value because it was entered into by only one licensee, Sirius XM, which provides its CABSAT service through only one affiliate, and solely as a promotional tool for its primary satellite radio business. He also describes the history of the PSS and CABSAT markets, explaining that no company has managed to operate a long-term profitable business based on its CABSAT service alone and that the CABSAT market is therefore an unproven and unstable market.

Mr. Del Beccaro next explains that SoundExchange's rate proposal, and the testimony meant to support that proposal by Dr. Wazzan, is fatally flawed because it even if the CABSAT rates were marketplace rates (they are not, as noted above), the PSS rates are set pursuant to the policy-based standard of Section 801(b) and it has been long established that reasonable rates under Section 801(b) are not the same as marketplace rates.

He also demonstrates that SoundExchange's proposal would frustrate the Section 801(b) policy factors applicable here, and shows the devastating effect it would have on Music Choice's residential audio business. Additionally, he notes that SoundExchange has failed to justify in any way its proposal that the PSS rate structure be radically changed, after two decades, from a percentage of revenue formula to a per-subscriber formula that would unfairly result in Music Choice paying an ever-increasing share of its revenue at a time when the MVPD marketplace is placing a lower value on sound recording performances.

He rebuts Dr. Wazzan's sole justification for adopting a per-subscriber rate – his belief that it may be possible that Music Choice gives preferential rates to its cable operator partners – by demonstrating that Dr. Wazzan has made several fatal errors in his analysis. First, those cable operator partners, together, control a very small minority of the voting and economic interest of the partnership. Second, Mr. Del Beccaro shows that the reason those partners have low rates is because they are also among the largest cable companies in the country, and gives examples of non-partner affiliates that have received lower rates than partners due to their relative size. He also demonstrates that the automatic annual rate increases in SoundExchange's proposal are unsupported and unwarranted.

Mr. Del Beccaro then explains the many reasons why SoundExchange's proposal that Music Choice pay a new, additional royalty fee for the ancillary internet transmission of its residential audio service to its subscribers must be rejected. He notes that the PSS license, unlike the SDARS license, explicitly allows a

PSS to expand onto additional platforms without being considered a new service, and that the legislative history of the provision creating the PSS license expressly states that a PSS may provide its service through internet transmissions as part of its PSS service. Mr. Del Beccaro also describes how Music Choice has included internet transmissions as part of its residential service since 1996, from the very first CARP proceeding through the past two CRB proceedings (and one SoundExchange audit), and that those transmissions have always been included within Music Choice's royalty payments under the PSS license. Not once in any of those rate proceedings or the audit did SoundExchange ever take the position that Music Choice needed to pay additional fees for its ancillary internet transmissions, even though it was well aware that Music Choice was making those transmissions. He also explains that any value created by the internet transmissions is captured in the revenue received by Music Choice, and therefore is included within the PSS royalty paid to SoundExchange as a percentage of that revenue.

Mr. Del Beccaro also testifies that the single CABSAT provider that negotiated the settlement creating the exclusion of internet transmissions from the CABSAT license, Sirius XM, does not offer internet transmissions as part of its CABSAT service, and therefore would not be impacted by agreeing to that exclusion. The only service that did provide internet transmissions as part of its CABSAT offering, Stingray, apparently stopped paying those separate or additional fees in 2015, even though it continued to make those internet transmissions.

He also rebuts Mr. Kushner's testimony about the alleged substitutional impact of the PSS, explaining that Music Choice is not a "streaming" service and demonstrating that by Mr. Kushner's own logic and as evinced by the fact that recording industry revenues increased dramatically and reached their historical peak during the first ten years after the PSS began operating, the PSS have increased, not decreased, the record industry's revenues.

Mr. Del Beccaro addresses the numerous changes SoundExchange proposes to the governing regulations and how each of them is needless, baseless, or prejudicial to Music Choice. Finally, he explains that GEO Group's rate proposal is not supported by any evidence or any economic or other rational basis, and that it would be even less reasonable than SoundExchange's proposal.

(2) Damon Williams, the Senior Vice President of Programming Strategy and Partnerships at Music Choice, presents further testimony demonstrating the promotional effect of the Music Choice residential audio service. By providing many examples of Atlantic business employees lobbying Music Choice for airplay, seeking out promotional opportunities for its artists (including every one of the artists identified by Mr. Kushner in his testimony as examples of important Atlantic artists), and thanking Music Choice for its help selling Atlantic recordings, he rebuts Mr. Kushner's absurd claim that Atlantic Records has "never viewed the PSS as major outlets for our music." That Atlantic's A&R, marketing and promotion departments devote so much effort and expense specifically to getting airplay and

other promotion on Music Choice's residential service is completely inconsistent with the self-serving testimony from Atlantic's legal department.

(3) Dr. Gregory Crawford, Ph.D., Professor of Economics and Director of Graduate Studies at the University of Zurich Department of Economics, again provides his expert opinion, this time regarding the myriad flaws in SoundExchange's rate proposal and the multitude of reasons why that proposal must be rejected in its entirety. He analyzes the testimony of Dr. Wazzan, exposing its many errors. Professor Crawford first testifies to the many reasons why the sole benchmark relied upon by Dr. Wazzan, the existing CABSAT rates, is unreliable and cannot be used to determine the PSS rates.

He first explores the genesis and history of the CABSAT rates, explaining that those rates have never been competitive marketplace rates, or even regulatory rates set by the Judges under the fair market, willing buyer-willing seller standard applicable to the CABSAT license. Instead, as Dr. Crawford explains, the CABSAT rates have always been the product of a litigation settlement between the entire recording industry on one side (negotiating collectively through SoundExchange) and usually only one licensee, Sirius XM on the other. In particular, the current CABSAT rates used by Dr. Wazzan as his sole benchmark were the product of such a settlement, and the agreement memorializing that settlement expressly states that the rates set by that agreement are not reflective of marketplace rates and even **directly prohibits SoundExchange from attempting to rely on the CABSAT rates as a benchmark in any rate proceeding, such as this one.**

Professor Crawford also explains that the CABSAT rates are not a reliable benchmark because the CABSAT offering by Sirius XM (the sole negotiating licensee) is insignificant to that company's overall business. The CABSAT service is not operated as a real business line but rather as a promotional expense to drive increased revenue for its primary business, satellite radio. Professor Crawford goes on to explain that none of the other few companies that have entered the CABSAT market have ever proven able to operate (or even interested in operating) a long-term profitable business solely from their CABSAT services. MTV entered the market, but left after only a few years. DMX entered the market, but only had one CABSAT affiliate and did that deal solely to obtain, as part of a negotiated bundle, significant satellite distribution savings for its primary commercial background music service. Even with that added benefit, DMX could not justify continued operations and recently exited the market.

And Stingray, the only other company ever to enter the CABSAT market, has only been able to do so by undercutting Music Choice's price. And even then, its market penetration has been limited only a tiny percentage of the MVPD market. Professor Crawford explains that Stingray's small share of the market consists almost entirely of smaller cable operators, who must pay the highest prices due to their size, and that it cannot expand its market presence significantly without taking on more of the large MVPDS at even lower rates. Professor Crawford notes that SoundExchange has failed to introduce any evidence of whether Stingray is currently operating at a profit from its U.S. CABSAT operations, and also

demonstrates that if Stingray were able to expand substantially into the MVPD market, it would be highly unlikely to do so on a profitable basis. This instability and lack of profitability in the CABSAT market further undermines its use as a reliable benchmark.

Professor Crawford also demonstrates that Dr. Wazzan has failed to account for many of the differences, including those noted above, between the actual CABSAT market and the PSS market at issue in this proceeding, and demonstrates that no PSS (or CABSAT) provider could profitably operate its service as a stand-alone business under SoundExchange's rate proposal. He also explains why, particularly given the history and legislative intent behind the PSS license and rate standard, reasonable rates must provide a sufficient return from a PSS to operate a profitable stand-alone business.

Professor Crawford rebuts Dr. Wazzan's and Mr. Orszag's claim that marketplace rates necessarily promote the first three policy objectives of the PSS rate standard, based upon both appellate precedent from early PSS rate litigation as well as established economic principles. He also demonstrates that, to the extent he bothered to do any, Wazzan's analysis of the Section 801(b) policy factors is severely flawed.

Professor Crawford also demonstrates that Dr. Wazzan's conclusions on a number of other topics are faulty as well: PSS rates should continue to be set as a percentage-of-revenue, they should absolutely include the right to retransmit PSS programming to subscribers over the internet, and the patterns of Music Choice's

rates paid by its cable partners are perfectly consistent with patterns of size discounting in the industry.

Turning to the testimony of Dr. Ford, Professor Crawford shows that, while Dr. Ford's analysis purports to opine on whether or not non-interactive services like the PSS are substitutional or promotional for other sources of recording industry revenue, he simply fails to present a compelling or credible opinion on this point. Professor Crawford shows that Dr. Ford's claims are unsupported by any empirical or other persuasive evidence. By contrast, counter-evidence on this question presented by Professor Crawford strongly suggests that Music Choice's PSS is net promotional, and that even a small promotional effect would lower significantly the rate that would arise in a hypothetical competitive market for PSS sound recording performance rights.

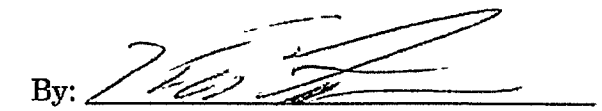
VOLUME II: MUSIC CHOICE EXHIBITS

Pursuant to 37 C.F.R. § 351.11 and the Judges' Orders, Music Choice submits the following exhibits, included in Volume II:

Exhibit No.	Sponsoring Witness	Description	Version
MC 42	David J. Del Beccaro	CABSAT Settlement Agreement	Public
MC 43	David J. Del Beccaro	UMG Recordings Services, Inc. and Music Choice Term Sheet – October 2016	Restricted
MC 44	David J. Del Beccaro	Residential Audio Projections Under SoundExchange's Proposed Rates	Restricted
MC 45	David J. Del Beccaro	Combined Projections Under SoundExchange's Proposed Rates	Restricted
MC 46	David J. Del Beccaro	Music Choice Correspondence with RIAA re: Internet royalties	Public

Exhibit No.	Sponsoring Witness	Description	Version
MC 47	David J. Del Beccaro	Press Release re: Stingray on AT&T	Public
MC 48	David J. Del Beccaro	Stingray Music channel lineup	Public
MC 49	David J. Del Beccaro	RIAA US Recorded Music Revenues by Format	Public
MC 50	David J. Del Beccaro	SDARS II Stipulation regarding Minimum Fee	Public
MC 51	David J. Del Beccaro	CARP Report Final Report excerpts regarding defensive audit provisions	Public
MC 52	Damon Williams	Updated list of artist promotional visits to Music Choice or on-site engagements 2013-2016	Restricted
MC 53	Damon Williams	Emails regarding B.O.B. promotion	Restricted
MC 54	Damon Williams	Recap of social media promotion with Sevyn Streeter	Restricted
MC 55	Damon Williams	Emails from an artist's PR manager soliciting collaboration	Restricted
MC 56	Damon Williams	Emails regarding a collaboration of artists and their studio visit	Restricted
MC 57	Damon Williams	Emails regarding a studio visit with an artist and with Atlantic representatives	Restricted
MC 58	Damon Williams	Emails regarding new singles for which Atlantic was either seeking new airplay or thanking Music Choice for current airplay	Restricted
MC 59	Damon Williams	Emails from Atlantic regarding Music Choice's role in a song's success	Restricted
MC 60	Damon Williams	Emails from Atlantic representatives lobbying Music Choice for airplay or thanking for help in promoting their artists and content	Restricted

DATED: February 17, 2017

By: 

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In the Matter of:	Docket No. 16-CRB-0001-SR/PSSR (2018-2022)
Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)	

MUSIC CHOICE'S AMENDED RATE AND TERM PROPOSAL

Pursuant to 37 C.F.R. § 351.4 and the Judges' Notice of Participants, Commencement of Voluntary Negotiation Period, and Case Scheduling Order dated March 14, 2016 and the Judges' Order for Further Proceedings and Case Scheduling dated June 28, 2016 (the "Judges' Orders"), Music Choice respectfully submits its amended Rate and Terms Proposal.

I. MUSIC CHOICE'S AMENDED RATE AND TERMS PROPOSAL

A. Rates

Pursuant to 37 C.F.R. §351.4(b)(3), Music Choice proposes that the Section 114 sound recording performance license rate for Music Choice be reduced to no higher than 5.6 percent of gross revenues as that term is currently defined in the applicable regulations. Because the ephemeral copies made by Music Choice have no

independent economic value, Music Choice proposes that the Section 112 ephemeral license fee be included within the performance royalty rate noted above.

B. Terms

Music Choice proposes that the terms and other regulations applicable to the PSS license be amended as follows:

1. Minimum Payment

Music Choice proposes that 37 C.F.R. §382.3(b) be amended to reference the minimum payment's applicability to both section 112 and section 114 royalties. The language Music Choice proposes is as follows:

(b) Each Licensee making digital performances of sound recordings pursuant to 17 U.S.C. 114 and Ephemeral Recordings pursuant to 17 U.S.C. 112(e) shall make an advance payment to the Collective of $100,000 per year, payable no later than January 20th of each year. The annual advance payment shall be nonrefundable, but it may be counted as an advance of the section 112 and section 114 royalties due and payable for a given year or any month therein under paragraph (a) of this section; Provided, however, that any unused portion of an annual advance payment for a given year shall not carry over into a subsequent year.

This change to the current regulations would more accurately reflect the minimum fee provision to which the parties agreed in the prior proceeding, in which they stipulated to applying the yearly minimum fee to both section 112 and section 114 royalties owed in that year.

2. Cost of Audit

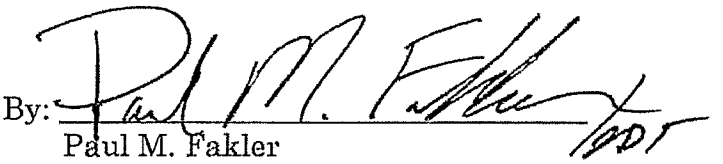
Music Choice proposes that the regulations regarding the cost of audits, 37 C.F.R. §382.6(f) and 37 C.F.R. §382.7(f) (or their analog if the relevant terms are moved or consolidated) be amended to provide that the Licensee shall bear the cost of an audit only in the case of an underpayment of 10% or more. The language Music Choice proposes is as follows:

37 C.F.R. §382.6(f) ***Costs of the verification procedure.*** *The interested party or parties requesting the verification procedure shall pay all costs of the verification procedure, unless an independent and Qualified Auditor concludes that during the period audited, the Licensee underpaid royalties by an amount of ten (10) percent or more; in which case, the service that made the underpayment shall bear the costs of the verification procedure.*

37 C.F.R. §382.7(f) ***Costs of the verification procedure.*** *The interested party or parties requesting the verification procedure shall pay for all costs associated with the verification procedure, unless an independent and Qualified Auditor concludes that, during the period audited, the Licensee underpaid royalties in the amount of ten (10) percent or more, in which case, the entity that made the underpayment shall bear the costs of the verification procedure.*

This proposed change would serve to harmonize the PSS license with the webcasting, SDARS, CABSAT and BES licenses, all of which utilize a 10% threshold before the cost of an audit is shifted to the licensee.

DATED: February 17, 2017

By: 

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WRITTEN REBUTTAL
TESTIMONY OF
DAVID J. DEL BECCARO

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WRITTEN REBUTTAL TESTIMONY OF DAVID J. DEL BECCARO

My name is David J. Del Beccaro. I am the President and CEO of Music Choice, and have run the company since I founded it in the late 1980s, as described in my Written Direct Testimony. I submit this Written Rebuttal Testimony to respond to various claims and arguments advanced by SoundExchange and the other copyright-owner participants in their Written Direct Statements in the above-captioned proceeding.

The CABSAT Rates Are Not an Appropriate Benchmark for the PSS

Based upon the testimony of Dr. Wazzan, SoundExchange and various other record industry entities (collectively "SoundExchange") rely on only one benchmark to support their PSS rate proposal: the current rates applicable to new subscription services offered through residential cable and satellite television providers, which SoundExchange calls the "CABSAT" services. The CABSAT rates cannot be used as a reliable benchmark to set rates for the PSS for a number of reasons. First, those

rates are not the product of any competitive marketplace transaction or even a judicial determination of fair market value, but rather come from a litigation settlement that expressly prohibits SoundExchange from attempting to rely on the CABSAT rates as a benchmark in any rate proceeding. Second, that settlement was a deal struck by a licensee that is not actively competing in the CABSAT market and had no rational business incentive to fight for a fair market rate. Third, the CABSAT market is not competitive or stable; there has never been a CABSAT licensee that has proven to operate a long-term profitable business from its CABSAT operations. And fourth, even if the CABSAT rates had been the product of a competitive marketplace transaction or the Judges' estimation of such a transaction, the PSS rates must be set pursuant to the Section 801(b) policy standard, which is fundamentally different from the marketplace standard applicable to the CABSATs. SoundExchange has not even attempted to adjust the CABSAT rates to account for the different rate standards.

The CABSAT Rates Do Not Reflect Fair Market Value

Having participated in several rate proceedings—before the CARP, the Judges, and the BMI rate court—my understanding of benchmarking is that the benchmark is supposed to have comparable buyers and sellers in a competitive marketplace transaction, and reflect fair market value in the benchmark market. The CABSAT rates do not meet any of these requirements. Those rates are the product of a settlement of the most recent CABSAT rate litigation between the entire recording industry, through SoundExchange (on one side), and only one

licensee, Sirius XM (on the other side). Remarkably, the settlement agreement itself contains a provision noting that the resulting rates and terms are not precedential because they are based on factors other than marketplace factors. That same provision expressly prohibits SoundExchange from attempting to rely on the CABSAT rates as a benchmark in any rate proceeding. The settlement agreement is attached as Exhibit MC 42. I cannot comprehend how SoundExchange could possibly ignore the plain language of this provision by submitting its PSS rate proposal based solely on the CABSAT rates. I also note that SoundExchange attempted to avoid producing this document in discovery and forced Music Choice to expend resources on filing a motion to compel. It was only after the Judges ordered SoundExchange to produce the CABSAT settlement agreement that we found out about this fatal provision.

Even putting aside the express prohibition on using them as a benchmark, the rates that Sirius XM was willing to settle for to avoid a multimillion-dollar litigation is not a reliable indicator of fair market value for CABSAT rights. Sirius XM is not an active participant in the CABSAT market. Sirius XM provides its CABSAT service to only one affiliate, DISH Network, and is not even trying to expand beyond that one affiliate. That is because it essentially gives the service away to DISH as a promotional tool to drive subscriptions to its real business, satellite radio. Thus, its one CABSAT account is not an actual business line for Sirius XM, just a promotional expense for a different business. Given this role, it is not surprising that Sirius XM's CABSAT service is a no-frills affair. Unlike Music

Choice, Sirius XM does not include internet or mobile app access as part of its DISH Network service, nor does it include a video on demand ("VOD") or linear music video channel. Nor does Sirius XM invest in designing an engaging on-screen display for the DISH service (as Music Choice does for its own service), given that such a display would not be useful for Sirius XM's real business of satellite radio in the car. Given that the whole point of its DISH offering is promotional, Sirius XM transmits only a subset of the same programming it uses for its satellite radio product. This also means that Sirius XM incurs very little cost to provide its CABSAT service, which allows it to give the service away at a very low price.

In light of these business realities of its CABSAT service, Sirius XM had no rational business incentive to litigate the last CABSAT proceeding. Even as a relatively small company with limited means, Music Choice spent over [ ] litigating the last PSS proceeding. I am confident that Sirius XM has spent a multiple of that on each of its SDARS proceedings. But even if it were to have put on a scaled-down case similar to Music Choice, Sirius XM could not have hoped to save enough on royalty expenses for a minor promotional program to justify the cost of litigation. Nor could it free-ride on any other licensee's litigation efforts, because it was the only licensee that petitioned to participate. Thus, not only would Sirius XM not be willing to litigate the case, its unwillingness to litigate greatly diminished its ability (or desire) to negotiate the settlement aggressively. Its only rational choice was to settle on the best terms it could quickly and easily get from SoundExchange.

As I have learned from decades of dealing with SoundExchange, that pressure to settle was not felt equally by the record industry. Unlike individual licensees, litigation through SoundExchange allows the record industry to spread rate litigation costs out over its many thousands of members, in rough proportion to the revenues those companies and artists receive from SoundExchange (given that the litigation fees come out of licensee royalty payments before those payments are distributed to the record companies and artists).

Summing up, in light of the realities of Sirius XM's CABSAT service in the context of its overall business, and the other negotiating dynamics described above, it would be unreasonable to view the CABSAT rates set in that settlement agreement as reflecting fair market rates that would have been negotiated in a competitive marketplace transaction by a company actively trying to operate a profitable CABSAT business. Nor does Sirius XM offer a robust CABSAT service that would be comparable to Music Choice's residential service. For these reasons alone, the Judges should reject SoundExchange's attempt to use the CABSAT rates as the benchmark to determine the PSS rates applicable to Music Choice.

None of the Other CABSAT Licensees Have Had Viable Long-Term Businesses From Their CABSAT Operations

Another reason why the CABSAT rates are not a reliable benchmark for reasonable rates is that they apply to an unproven and unstable market. In the almost twenty years since the DMCA created the PSS / CABSAT distinction, no CABSAT service has ever operated a significant, long-term, viable business based on that service alone. Indeed, even with respect to the PSS, Music Choice is the only

company that has been able to operate a successful service. As noted above, Sirius XM essentially gives away its CABSAT service not as a business line, but as a marketing expense. Similar to Sirius XM, both DMX and Muzak provide their respective CABSAT and PSS services to only one affiliate each, at a fraction of the rates commanded by Music Choice—not to operate those services as a viable business line, but to gain significant benefits for their actual businesses, *i.e.*, commercial background music services. MTV entered the market for a few years, thinking it could leverage its brand and existing operations into a viable CABSAT service, but failed, and exited the market. Finally, although Stingray has entered the market by leveraging the sunk costs from its profitable Canadian music operations, after six years of undercutting Music Choice's prices Stingray has managed to get only one large MVPD affiliate, and even with that affiliate has failed to expand beyond a very small percentage of the overall MVPD market.

In the 1980s and 1990s, Muzak and AEI (a predecessor to DMX) operated commercial background music services using their own satellite systems. Muzak was by far the larger commercial background music distributor. AEI concentrated on more personalized commercial background music accounts, which provided higher revenue. The satellite receiver systems needed at each business location cost the distributors or dealers around $800 (including hardware and installation). Muzak and AEI also each had very high costs associated with maintaining their own respective dedicated satellite platforms, including having to create broadcast centers, playback facilities, and uplink facilities. This meant that in order to recoup

their investment, Muzak and AEI had to charge background music customers high monthly fees and lock them into long-term deals.

Music Choice launched its residential service on DIRECTV in 1994 and began establishing a commercial background music dealer network in 1995. Given the huge subscriber volumes and commercial background dealer networks associated with DIRECTV, we were able to install satellite receiver systems at commercial background music customer locations for under $300, and the price went down from there. We were thus able to offer a lower price with a shorter-term contract, which was very compelling. We quickly grew to almost 100,000 commercial subscribers.

DISH launched after DIRECTV, in 1996. When we bid for that business, we were in intense competition with DMX (which was not a significant commercial background music supplier at that time) and Muzak. DMX and Music Choice, of course, were primarily interested in DISH's residential business. Muzak was fighting for its life at the time, because much of our growth had come at its expense. In that context, Muzak agreed to basically give away its residential business to DISH in exchange for a long-term deal to use DISH's satellite infrastructure for Muzak's more important commercial background business. This allowed Muzak to shut down its expensive, dedicated commercial satellite platform and use DISH's playback, uplink, and satellites for free. I do not know for certain the exact price that Muzak received from DISH at that time, but in bidding for the business

recently it has become clear that the current price (twenty years later) is [ ] per subscriber per month.

This was the status quo until our affiliation deal with DIRECTV expired in 2005. By that time, DMX had merged with AEI and was now a major player in the commercial background market. In fact, by that time, DMX's limited residential business was in freefall. Given that Muzak was on DISH, DMX/AEI made a big play to secure the DIRECTV business. It did this by offering DIRECTV the same kind of deal that Muzak struck with DISH, namely trading an almost free price on the residential service for satellite infrastructure benefits accruing to DMX/AEI's far more important commercial background business. We later came to learn that DMX's residential price on DIRECTV was [ ] per subscriber per month. In fact, DMX lost so much money on the residential side of this deal that [[ ]]

Of the original three PSS, Music Choice is the only one left actually competing for business. Both Muzak and DMX went into bankruptcy, with only Muzak emerging as the same PSS company (as the company acquiring the DMX name after the original DMX's bankruptcy was deemed not to be a PSS). DMX attempted to continue providing its service to DIRECTV while paying the CABSAT rates, but the economics were so unfavorable that [ ] it transferred the obligation to its now-sister company Muzak, so that Muzak could at least lose less money by paying the PSS rates.

Muzak's only affiliate (other than taking over the DMX contract with DIRECTV) remains DISH. So DMX is completely out of the CABSAT market, and Muzak is not even trying to get any additional business. It is only in the market because of the cost savings its parent company, Mood Music, gets for its primary commercial background business, as described above, from providing the DISH and DIRECTV services.

The rest of the CABSAT market has not fared any better. Since the CABSAT / PSS distinction was created in 1998, there have been no market entrants that have proven able to operate a viable long-term business. As noted above, Sirius XM and DMX (until it recently exited the market altogether) have only marginally participated in the market, each serving only one affiliate almost for free to get significant benefits for its different, primary business. MTV attempted to operate a CABSAT service, entering the cable market in 2007, but decided to exit the market in 2010 (and had completely ceased operations by 2011).

The only other company to operate as a CABSAT in all that time is Stingray. Stingray was able to enter the market only because it already had a significant residential audio service in Canada and could leverage many of its infrastructure and sunk expenses from that service to provide essentially the same service in the United States. For the past six years, Stingray has attempted to get a foothold in this country by drastically undercutting our prices to try to "buy" the business. Even with this strategy, we are typically able to keep our affiliates at a higher price than that offered by Stingray because our service is recognized as superior.

Although Stingray has managed to take some business away from us based solely on price, after six years it has been able to secure carriage on only one large MVPD, AT&T, and its overall MVPD market share is very small, at approximately [ ]. Stingray's limitation of its market penetration thus far to smaller cable operators has made it easier for Stingray to endure the absurdly high CABSAT rates because, as I discuss further below, the smaller operators pay significantly higher rates. But this also means that it will be highly unlikely for Stingray to scale up in a way that would allow it to be profitable. It has reached the point of diminishing returns, where only the addition of larger MVPDs will materially increase its revenues. But to continue undercutting the existing prices with medium and large MVPDs by a sufficient amount to overcome its inferior quality, it will have to offer rates so low that it would likely lose money on an incremental basis.

The only way this strategy could lead to long-term profitability would be if Stingray were to *both* (1) completely drive Music Choice out of the market and (2) then use the resulting monopoly to drive prices back up. Given Stingray's limited success thus far in taking significant business away from Music Choice, the first step seems highly unlikely unless this proceeding puts us out of business with a high rate. But the second step would be totally impossible, given the market dynamics of the MVPD industry described in my Written Direct Testimony. Keep in mind, to provide a viable residential audio service, Stingray (like Music Choice) must also provide a bundled video service for no, or at best a nominal additional charge to the MVPDs. And (also like Music Choice) Stingray must pay an even

higher royalty fee for the video rights, which must be negotiated directly with the record companies. When the cost of the video rights is added to the CABSAT rate, and given how low Stingray would have to price its combined service to undercut our prices with the larger MVPDs (which given industry consolidation comprise an increasingly greater share of the market), it is highly unlikely that its revenue could exceed that total (CABSAT plus video) royalty burden.

The Section 801(b) Rates Are Not the Same as Marketplace Rates

The CABSAT rates have never been evaluated, set, or adjusted by the Judges. Every time that a rate proceeding has been instituted, the royalty rates and terms were settled by agreement, and therefore the Judges were precluded from independently evaluating the rates to determine whether they satisfied the willing buyer / willing seller, fair market value standard applicable to the CABSAT license. And, as noted above, the CABSAT rates negotiated by Sirius XM were certainly not indicative of fair market value, but instead were much higher than fair market value. Even if the CABSAT settlement rates did reflect fair market rates, however, they would have to be evaluated and adjusted based upon the Section 801(b) policy factors.

As I explained in more detail in my Written Direct Testimony, Music Choice launched its business long before there was any performance right for sound recordings under U.S. copyright law. The pre-existing investments and business operations of Music Choice and the other PSS without any expectation of having to pay sound recording royalties was a motivating factor in Congress's decision to

create a statutory license with rates set pursuant to the Section 801(b) policy factors when it first created the sound recording performance right. It was those same fairness concerns and consideration for the business expectancies of the original, pioneering digital music companies that led Congress to create the PSS designation and grandfather the PSS under the policy-based standard when it decided to move any future market entrants, such as the CABSATs, to a fair market value standard.

SoundExchange, through Mr. Orszag and Dr. Wazzan, argue that marketplace rates automatically satisfy at least the first three policy factors, but that claim is clearly wrong. First, that argument is flatly contradicted by prior appellate rulings of the Librarian of Congress and the D.C. Circuit. At the first appellate level of the very first PSS rate proceeding, the Librarian rejected similar arguments that Section 801(b) rates should be the same as marketplace rates, holding that the standard for setting the PSS rate "is not fair market value." *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings (Final Rule and Order)*, 63 Fed. Reg. 25,394, 25,399 (May 8, 1998) ("Librarian's PSS Determination"). The Librarian flatly rejected the argument, made by SoundExchange's predecessor RIAA, that the PSS rate had to be consistent with market rates, holding that the PSS rate "need not mirror a freely negotiated marketplace rate • *and rarely does* • because it is a mechanism whereby Congress implements *policy considerations which are not normally part of the calculus of a marketplace rate.*" *Id.* at 25,409 (emphasis added).

At the second level of appeal, the D.C. Circuit affirmed on this point, holding that "RIAA's claim that the statute clearly *requires* the use of 'market rates' is simply wrong." *RIAA v. Librarian of Congress*, 176 F.3d 528, 533 (D.C. Cir. 1999). The court went on to note that the PSS rate standard "does not use the term 'market rates,' nor does it require that the term 'reasonable rates' be defined as market rates. Moreover, there is no reason to think that the two terms are coterminous, for it is obvious that a 'market rate' may not be 'reasonable' and vice versa." *Id.*

Even in the absence of these prior rulings, SoundExchange's argument should be rejected on common-sense grounds. Congress purposefully grandfathered the PSS under the policy factors at the same time that it created the new, fair market standard for later market entrants. It would not have bothered doing so if it intended for the Judges to simply ignore the first three factors by treating them as automatically incorporated within a market rate. Nonetheless, Dr. Wazzan fails to make any adjustment for any of the policy factors, based on his unsupported and incorrect belief that marketplace rates always already promote the first three policy factors. Though he justifies his failure to make adjustment on his beliefs about the inherent characteristics of marketplace rates, he acknowledges that the CABSAT rates *are not* marketplace rates. So even if he were right about marketplace rates (he is not), such a rule has no applicability to the CABSAT rates by his own admission.

Even more troubling, Dr. Wazzan argues at length in other parts of his testimony that Music Choice's existing rate cannot be used as a starting point for the policy factor analysis because for certain rate periods the rates were set as the product of a litigation settlement between Music Choice and SoundExchange. Wazzan WDT, p. 16. Indeed, he goes so far as to opine that "there are many reasons why a settlement lacks reliability as to the true value of a royalty rate." *Id.* Given the strength of his opinion, I can only assume he was not aware that the CABSAT rates are the product of a similar settlement. Indeed, the CABSAT rates have *never* been set by a CARP or the Judges. They have been set exclusively by a series of settlement agreements, quite unlike the PSS rates, which were originally set by the CARP pursuant to the Section 801(b) policy factors and were most recently adjusted by the Judges pursuant to those factors. And, as noted above, the settlement agreement producing the current CABSAT rates expressly prohibits SoundExchange from relying on those rates as a benchmark in this proceeding.

SoundExchange's Proposed Massive Rate Increase Would Not Promote the Section 801(b) Policy Factors

As demonstrated above, SoundExchange's sole benchmark, the CABSAT rates, cannot provide a reliable starting point for adjusting the PSS rates. But even momentarily ignoring that fatal flaw, the rates proposed by SoundExchange would undermine all four of the Section 801(b) policy factors and could not be considered reasonable.

SoundExchange Has Failed to Justify Its Proposed Change to a Per-Subscriber Rate Structure or Its Automatic Annual Rate Increases

SoundExchange seeks to upend over twenty years of PSS royalty history by eliminating the percent of revenue royalty formula and replacing it with a per-subscriber rate structure. SoundExchange does not advance any reason for this radical change, other than Dr. Wazzan's claim that "it is not clear [to Dr. Wazzan] that [Music Choice's] partner prices are the result of arms-length marketplace transactions" and therefore "[c]harging a per-user fee is more likely to approximate rates achieved through the marketplace." Wazzan WDT, pp. 37-38. As further demonstrated by Professor Crawford in his Written Rebuttal Testimony, Dr. Wazzan's lack of clarity on this issue is likely due to at least two errors. First, he misreads the Music Choice documents he cites for his claim that Music Choice is majority owned by cable companies (completely false: cable companies in the aggregate own less than a one-third interest) and his chart lists incorrect subscriber counts for certain cable companies. Second, he apparently failed to investigate or consider the historical sizes of certain Music Choice affiliates at the time they entered into their agreements with Music Choice. As I testified in my Written Direct Statement, and as the Judges previously held after the hearing in SDARS II when SoundExchange made these same false allegations, Music Choice's affiliation deals with its cable company partners have always been arms-length deals.

With respect to Dr. Wazzan's claim that Music Choice is majority-owned by cable companies; this claim is flatly false, and I have no idea how he could have come to that belief. As I testified in my Written Direct Statement, cable companies

in the aggregate hold less than a one-third interest in Music Choice, with each individual cable company holding a fraction of that share. More specifically, our cable partners' aggregate share of economic interest in the company is [[redacted]], and their aggregate voting share is [[redacted]]]. Charter Communications holds a [[redacted]] economic and [[redacted]] voting share. Comcast holds a [[[redacted]]] economic and [[redacted]] voting share. Cox controls a [[redacted]]] economic and [[[redacted]]] voting share. Those are the only interests in Music Choice owned by cable companies. The super-majority of both economic and voting interest in Music Choice is controlled by non-cable companies, including companies affiliated with record companies.

As I have previously testified in both this proceeding and SDARS II, Dr. Wazzan's claim that Music Choice charges its partner affiliates lower rates than we would have charged them if they had not been partners is simply not true. Music Choice negotiates with these partner companies in the same manner it negotiates with any other MVPD, and the prices Music Choice is able to obtain in those negotiations are driven in largest part by the other company's size (*i.e.*, its number of subscribers) at the time of the negotiation, which determines its leverage. Music Choice's MVPD partners are, and were at the time their contracts were signed, among the largest cable operators in the country. Because Music Choice gets paid based on a cable company's number of subscribers, the largest companies provide the lion's share of Music Choice's revenue and therefore have the most leverage,

enabling them to negotiate the most favorable prices.[1] In fact, if Music Choice had not been carried by Comcast or Time Warner, it likely would not have been a viable service. That is why Music Choice's partners have low rates.

Negotiations may also be colored by a customer's level of commitment to Music Choice, as reflected by the length of term of the agreement or level of distribution commitment. For example, Music Choice might be able to support a slightly lower price for a customer that signs a long-term contract, agrees to carry more of Music Choice's services, or offers Music Choice better positioning in an important market. But size is by far the most important consideration.

As a preliminary matter, in his testimony Dr. Wazzan uses an out-of-date source for subscriber numbers and therefore his chart does not reflect recent industry consolidation. He also makes several errors in his chart, mixing up certain companies' subscriber counts listed on his source document. In any event, the accurate figures are as follows: Comcast is the largest cable operator, with over 20 million subscribers. Charter is the second largest cable operator, having completed its recent acquisitions of Time Warner Cable and Bright House, with almost 17 million subscribers. Charter acquired its ownership stake in Music Choice through its acquisitions of Time Warner Cable and Bright House. Prior to being acquired by Charter, Time Warner Cable was the second largest cable operator, with approximately 13 million subscribers, far more than the 3.5 million listed in Dr.

[1] It is also unsurprising that the largest companies are the ones able to afford ownership stakes in other companies, such as Music Choice.

Wazzan's chart. With respect to its third cable partner, when Music Choice's contract with Cox was negotiated in 2005, Cox was the third-largest cable operator in the country, after Comcast, Time Warner, and Continental. Cox has since shrunk to roughly 3.5 million subscribers (Dr. Wazzan seems to have incorrectly attributed this number to Time Warner in his chart), but Cox [[ ]].[2]

Because of their size, and thus their leverage, these three companies were able to extract relatively low prices, leaving Music Choice operating on thin margins from those deals. But this negotiating dynamic is true regardless of whether a company holds a partnership interest in Music Choice. For example, in Music Choice's contract with [ ] In more recent times, Music Choice has made [[ ]]. Music Choice has also entered into negotiations with various [[ ]]

[2] Cox also has also historically been one of Music Choice's most committed customers: for example, it [ ]. This is of course another factor in Music Choice's negotiations with Cox.

[redacted].

These basic bargaining dynamics are unavoidable. Music Choice is paid on a per-subscriber basis. Therefore, the companies with the most subscribers have the most revenue to offer Music Choice and, correspondingly, the greatest bargaining power. Negotiations with the companies that hold that power, *i.e.* the largest MVPDs, are very difficult and often take two-and-a-half to three years to complete. There is no need, and in fact no room, for favoritism on the basis that a company holds a partnership interest in Music Choice.

Moreover, any such favoritism would make no sense, at several levels. First, as detailed above, neither Charter, Cox, nor Comcast own anything approaching a controlling interest in Music Choice and therefore could not hope to get Music Choice to provide them preferential treatment on an individual level. Second, even if the three cable company partners agreed amongst themselves to seek combined preferential treatment, the non-cable partners of Music Choice, which own over two-thirds of the partnership, would have no reason to agree to give the cable company partners below-market rates. The three cable company partners are Music Choice's largest customers and provide the bulk of its revenue; cutting their rates below arms-length rates would only harm Music Choice and reduce its value, which is not in the interest of any of the partners, but especially the non-cable-company partners. There is no potential benefit that goes to any of the non-cable partners other than the revenues generated from these deals. They do not receive the service

and there are no intangible benefits to them. So any preferential treatment of the cable partners would come directly out of the non-cable partners' pockets with no offsetting gain. Finally, for essentially the same reasons, I would have no incentive to, and would not, agree to such terms because they would be detrimental to both Music Choice and its partners.

Even putting aside SoundExchange's failure to justify its proposed radical change in rate structure, moving to a per-subscriber fee would be unfair to Music Choice. As discussed in my Written Direct Testimony, Music Choice has seen the per-subscriber rates it can obtain from MVPD affiliates consistently decrease over time due to a variety of marketplace dynamics. During that time, the relative value of sound recording rights to the value of our overall service has not increased. Moving from a percentage of revenue to a per-subscriber formula in this environment is not only unjustified, it would impose an additional, back-door rate increase, forcing Music Choice to pay an ever-increasing percentage of its revenue for the exact same rights at the same time as the marketplace (via the MVPDs) is placing a lower value on those rights.

Even worse than its requested change to a per-subscriber rate structure, SoundExchange has provided no justification whatsoever (not even a flawed one) for the 3% annual rate increases included in its proposal. As the Judges recognized in the recent Webcasting IV determination, there is no justification for such automatic rate increases, even when charging a flat fee per-performance (or per-user). Of course, one of the benefits of the percent of revenue structure for the PSS royalty is

that it automatically adjusts for any factor that would increase revenues, including inflation. [[redacted]]

SoundExchange's Proposed Rates Would Have a Devastating Effect on Music Choice and Impede the Policy Objectives of Section 801(b)

Even before considering the policy objectives of Section 801(b), SoundExchange's proposed massive rate increase, which would raise our sound recording royalty fees to almost [redacted] of revenue, bears no relationship to rates that would be negotiated in a competitive marketplace. Recently, in our negotiations with UMG (the largest major record company with massive market power) for music video rights, UMG sent us a term sheet in which [redacted] A copy of that term sheet is attached hereto as Exhibit MC 43.

UMG's request [redacted] is notable for a few reasons. First, UMG asked for this [redacted]

[redacted]]] Of course, we did not and would never agree to this proposal. As demonstrated in my Written Direct Testimony, even the existing rate threatens Music Choice's long term viability. Music Choice could never voluntarily agree to [redacted]]]. But UMG clearly felt that [redacted].

Given that SoundExchange's rate proposal is wildly higher than any possible competitive fair market rate, it should be no surprise that its proposed rate would also impede the policy objectives of Section 801(b). As I explained in my direct testimony, Music Choice's financial condition has significantly deteriorated over the current rate period, due largely to changes in the MVPD marketplace and the rate increase from SDARS II.[3] Consequently, even retaining the 7.5% rate implicit in the SDARS II determination would not afford Music Choice "a fair income under existing economic conditions," *see* 17 U.S.C. § 801(b)(1)(B), as I demonstrated in my direct testimony. *See* Del Beccaro WDT, pp. 19-33. Using the same methodology[4] I

[3] I note that this MVPD marketplace for agreements with programming providers like Music Choice is closer to a real, competitive, market than the CABSAT market and in the MVPD market the value of music companies' music content (as reflected in rates paid for music channels) is decreasing. The argument that we should have to pay more when consumers are valuing the content less is absurd.

[4] Music Choice does not receive daily or individualized subscriber counts from its affiliates, but typically receives aggregate subscriber counts at the beginning and end of each month. Consequently, we could not compute the royalty according to SoundExchange's proposed regulations, which require payment for every subscriber who receives the service for any part of each month. [redacted], and these charts computed the royalty due on that basis as well. These charts also exclude the additional webcasting fees sought by SoundExchange. As noted below, Music Choice does not have the data necessary to track individual performances and therefore cannot compute what the additional webcasting fees

previously used in my Written Direct Testimony to prepare financial projections under the current rate, *see* MC Exs. 10 & 11, I have prepared similar projections assuming SoundExchange's proposed escalating per-subscriber rates and attach them as Exhibits MC 44 and 45.

The effect of SoundExchange's proposal would be disastrous. Immediately upon taking effect, our payments to SoundExchange would increase [[ ]. *See* MC Ex. 44, p. 2. When our audio service is considered in isolation, we would take a projected annual net income loss of over [ ] increasing to almost [ ] by the end of the upcoming rate period. *See id* p. 6. If the overall bundled residential service (including video) is considered, the results are slightly better, *see* MC Ex. 45, p. 6, but due solely to [ ]. *See* Del Beccaro WDT, p. 27. In any event, even with [ ] the combined residential service would be highly unprofitable, with an annual net income loss of over [ ] in 2018, losses continuing through 2021, and a small positive net income of just over [ ] in 2022 (again, driven solely by [ ]]. Thus, in no way would

would be. Whatever those fees would be, and given that almost twenty years into the existence of the webcasting market no webcaster has ever had a profitable year, I can be certain that adding the webcasting royalty burden would drive Music Choice's performance materially lower, even with minimal usage.

SoundExchange's proposal permit us to earn a fair income under existing economic conditions.

Music Choice, on the other hand, is not seeking a handout. Our biggest substitutional competitor is, and has always been, terrestrial radio, which pays nothing to the record companies. This has been a significant competitive hurdle to overcome. Even under our own proposal of 5.6% of revenue for the upcoming rate period, we still project losing money on the residential audio business every year. What that rate would do, however, is give us a fighting chance. We currently project a [ ] on the audio segment in 2017, but a reduction in the PSS rate to 5.6% for the upcoming period would allow us to project [[ ] on that segment in 2018. That [ ] As I mentioned, our video advertising revenues [ ]] SoundExchange's proposal would make all of this completely infeasible.

All that Music Choice seeks through its proposal is a meaningful opportunity to earn "a fair income under existing economic conditions," as Congress intended—no more, and no less. As I explained in my direct testimony, the current rate does not, and would not, accomplish that goal. SoundExchange's proposal, which

translates to a colossal increase, would not only deprive Music Choice of a fair income, but would almost certainly put the company out of business entirely.

For all the same reasons discussed in my Written Direct Testimony as to why the existing rate would impede the other policy objectives of Section 801(b), the massive increase requested by SoundExchange would impede those objectives to an exponentially greater degree.

Music Choice's Provision of Its Audio Channels to Subscribers Through the Internet Has Always Been Included in the PSS Rate and Should Remain So

In addition to seeking a massive rate increase that would have dire consequences for Music Choice, as discussed above, SoundExchange asks that Music Choice pay an additional royalty for any transmissions to its subscribers through the internet, at the same rates paid by commercial webcasters. This part of SoundExchange's proposal must be rejected for several reasons.

As an ancillary part of its residential music service, Music Choice subscribers have had access to our audio channels through internet transmissions for almost the entire history of the company, beginning in 1996. Initially, the channels were simulcast over a web interface and eventually we added access through mobile apps, but at all times access to these simulcasts have been limited to authenticated subscribers who received and paid for the Music Choice service. Music Choice has always viewed these internet-based transmissions as an integrated part of the residential audio service, and a minor part at that. Usage has always been very

modest, and aggregate listening through our internet transmissions is less than [redacted] of our overall usage.

Given that we started offering these transmissions as part of our residential audio service in 1996, it has been part of our service for over twenty years, from the time of the first CARP proceeding through the past two PSS rate proceedings and one audit that SoundExchange conducted. SoundExchange never argued in any rate proceeding or the audit that these internet transmissions were not (or should not be) covered by the PSS rates in effect during those periods. SoundExchange's failure to make this claim in all that time was surely not due to any lack of notice on its part. When we announced our intent to introduce various enhanced features of our broadband internet transmissions (some of which we ultimately abandoned), RIAA (then the parent of SoundExchange) noticed those announcements and sent us a letter, initially taking the position that Music Choice's internet transmissions were outside the scope of the PSS license and insisting that a new rate needed to be set for those transmissions. I responded, explaining that the PSS license, unlike other statutory licenses, expressly allowed Music Choice to expand its subscription service into new transmission media so long as the general character of the music channels did not change. RIAA responded in turn, initially keeping to its position that the internet transmissions were not part of the PSS or covered by the existing rate, but I again responded with further explanation of why the internet transmissions were included within the existing license and royalty fee. Copies of this correspondence are attached hereto as Exhibit MC 46.

After that letter, RIAA dropped its claims, and when we were later audited by SoundExchange for our PSS payments, it never once raised the claim that we need to pay extra for the internet transmissions. Consequently, we continued to invest in rolling out and improving these features for our subscribers. We did so in reliance on RIAA's (and its subsidiary SoundExchange's) acquiescence to our position. Our PSS license payments have included these internet transmissions since 1996. The internet transmissions are not a separate service; they are provided to cable subscribers as an extension of the residential cable audio service, all for one price. To the extent those transmissions have value, that value has (at least since 1996) been factored into the fee that we negotiate with our MVPD affiliates, and SoundExchange has been paid for that value through the percent of revenue rate formula. It is therefore both puzzling and disturbing to me that SoundExchange would now, so many years later, suddenly take the position that Music Choice must pay an additional, new fee for something that has always been included in our PSS payments.

The fact that our internet transmissions are included within one bundled fee received from the MVPDs is not unique to Music Choice. Based upon my experience in the industry for almost thirty years, programming providers in the MVPD market do not typically get paid an extra fee for internet transmission of their television channels. Like Music Choice, other programming providers get one fee, with everything, including internet transmissions, valued as a package in one price no matter how the cable or satellite subscriber receives the signal. MVPDs do not

that is separately licensed directly from the record companies. Because our entire residential service is made available to subscribers through our website and app, those video channels and VOD service are also made available. But, just like with the television component of our service, the video portion of our service is separately licensed, and Mr. Bender must be aware of that fact or certainly could have been if he had ever asked Music Choice or any of SoundExchange's major label members.

Mr. Bender's comparison of Music Choice to Sirius XM's subscription webcasting service is similarly misleading. First, Sirius XM does not provide webcasting as part of its CABSAT service to DISH subscribers. It provides it as an extension of its primary satellite radio service at an added fee. Crucially, unlike the PSS license, the SDARS license does not allow Sirius XM to expand into new platforms or transmission media as part of its SDARS service. This is a fundamental difference between the two licenses and is built into the statute. Congress clearly intended to treat the two categories of licensees differently, likely because (unlike the SDARS) the PSS had been actually operating their services for years prior to the change to the willing buyer / willing seller standard and therefore had a greater entitlement to protection against disruption of those businesses. Thus, the fact that Sirius XM must pay subscription webcasting fees for its webcasting service is neither surprising nor relevant.

I also note that the only reason that any ancillary internet transmissions are not included within the CABSAT rate is that certain of those transmissions are excluded from the CABSAT license by the regulations. But those regulations are

only drafted that way because of the litigation settlements with Sirius XM. There is no reason in the statute why the CABSAT license could not include all ancillary internet transmissions. As I explain above, that settlement is not reflective of an actual competitive marketplace agreement for various reasons and therefore this exclusion of certain internet transmissions in the CABSAT regulations also cannot be used as a reliable benchmark to require the PSS to pay additional internet fees. But SoundExchange's proposal should be rejected for another compelling reason: Sirius XM had an additional incentive to agree to this exclusion. It would have no impact on Sirius XM whatsoever because Sirius XM does not provide website or app access as part of its DISH CABSAT service.

Yet another reason for the Judges to reject SoundExchange's proposal is that they propose that we pay the same rates paid by subscription webcasters pursuant to their statutory license. This makes no sense. First, the commercial subscription webcasting rate was set pursuant to the willing buyer / willing seller standard, which as noted above is fundamentally different from the Section 801(b) policy standard, and Dr. Wazzan has made no effort to adjust or analyze those rates under the policy standard. The nature of Music Choice's ancillary internet transmission of its residential audio channels is fundamentally different from that of a subscription webcaster, as are the various cost structures and demand characteristics of the two types of services. As I noted above, our television subscribers do not pay any discrete or additional charge for the internet transmissions, nor do our MVPD affiliates who get our television service pay us any separate fee for the internet

transmissions made by their television subscribers. Dr. Wazzan does not even consider any of these differences, much less account for them.

A further reason why SoundExchange's request for additional royalties for internet transmissions must be rejected is that we do not receive the data necessary to track individual performances, which would be required for Music Choice to calculate and pay the per-performance rates proposed by SoundExchange. The data we receive regarding the internet transmission of our audio channels only allows us to track certain aggregate listening statistics by channel, not individual users or the specific songs they listen to. So even if the Judges were to implement SoundExchange's proposal, we could not compute the royalties or provide the necessary listening data.

Finally, SoundExchange's proposal to require additional and separate fees for internet transmissions should be rejected because the imposition of such new fees would not promote any of the four policy factors of Section 801(b). As demonstrated above and in the testimony of Professor Crawford, SoundExchange is already requesting a massive rate increase for the PSS license, which contravenes all four of the policy factors. Further adding to Music Choice's royalty load through this additional fee, in any amount, would only further undermine each of those policy factors. Additionally, the imposition of an entirely new royalty obligation, especially on a new, per-performance basis when Music Choice does not have the data necessary to track individual performance, would be highly disruptive under the fourth factor.

In summary, there are several reasons why the Judges should reject SoundExchange's request to impose new and additional royalty fees upon Music Choice for internet transmissions that have been included within the PSS fees for over a decade. Each of those reasons should be independently sufficient to deny SoundExchange's request. Cumulatively, they are fatal to that request.

Stingray Has Been Providing Similar Internet Transmissions For the Past Several Years and Apparently Has Not Paid Webcasting Royalties Since 2014

From my review of the public briefs and Orders issued by the Judges in connection with a discovery dispute in this matter, I understand there is some question about whether Stingray has been providing internet transmissions to its CABSAT subscribers without paying webcasting royalties for those transmissions.[5] Particularly, in SoundExchange's sur-reply brief, it asserts that Stingray paid webcasting royalties only during 2013 and 2014. SoundExchange Public Sur-Reply Brief, filed January 26, 2017, pp. 2-3; Declaration of Brieanne Jackson, p. 2. If this is true, then there can be no question that Stingray has been providing the same kinds of internet transmissions to its CABSAT subscribers as Music Choice provides to its PSS subscribers, without paying additional webcasting royalties for those transmissions.

Stingray has, for the past several years, provided internet transmissions of music channels to its CABSAT subscribers, both through its website and through

[5] As I note above, any webcasting payments by Sirius XM, the only other CABSAT licensee in the market, are irrelevant. Sirius XM does not provide its webcasting service to DISH subscribers as part of its CABSAT service.

mobile apps and apps on digital set-top boxes. Although the features of its website and app transmissions have changed over time (as have Music Choice's), its use of the internet to provide its service to subscribers through its website and/or apps has been constant over the past few years. Stingray's internet transmissions certainly did not cease in 2015. To the contrary, when Stingray first launched on AT&T in late 2014 and early 2015, its channels were available to AT&T subscribers only through its app. Attached as Exhibit MC 47 is a copy of a press release dated October 29, 2014, announcing the launch of the Stingray Music app on AT&T's U-verse set-top box. The press release notes that the channels will be available only through the app and not available directly on the television listing until March of 2015 (although a larger set of channels would remain available through the app after that time). Attached as Exhibit MC 48 is a copy of the Stingray Music Channel Lineup on AT&T U-verse TV, with a 2015 copyright date, showing all of the channels available through the app.

In addition to the AT&T U-verse app, Stingray has had a mobile app for iOS and Android devices in the market during 2015 and 2016, through which any of its cable subscribers could access its audio channels. So, there can be no question that Stingray was making internet transmissions to its subscribers similar to those made by Music Choice during 2015 and 2016. Putting aside the fact that the PSS statutory license specifically allows Music Choice to make these transmissions as part of its PSS, which the CABSAT license does *not* allow Stingray to do, if Stingray stopped paying separate webcasting royalties for those transmissions, that raises

serious additional questions about SoundExchange's claims and Dr. Wazzan's assumptions underlying his view that Music Choice should be forced to pay additional webcasting fees.

Music Choice Is Not a Streaming Service and Has Increased, Not Decreased, Record Industry Revenues

In his direct testimony, Michael Kushner seems to suggest that Music Choice is somehow responsible for a decline in the record companies' revenues. Mr. Kushner is mistaken. His fundamental error lies in his inclusion of Music Choice in a sweeping definition of "streaming" services.[6] According to Mr. Kushner, "as recently as 2003 the recording industry derived almost all its revenue from the sale of physical products," but "sales of physical products have fallen steadily since their high in 1999." Kushner WDT, p. 4 ¶ 10. Mr. Kushner attributes this decline to online piracy, competition from television, movies, and video games, and a change in consumer preferences toward downloads and "streaming." *Id.* Notably, Mr. Kushner provides no evidence that "streaming" is actually a *cause* of the contemporaneous decline in the record companies' revenues since 2000, rather than merely correlated with that decline. As mentioned above, Mr. Kushner himself expressly identified several possible alternative causes, and there may be others.[7]

[6] "In this testimony, I use the term 'streaming' to refer to all delivery of public performances by means of digital audio transmissions, including on-demand streaming, noninteractive Internet streaming, and transmissions by the SDARS and PSS." Kushner WDT, p. 5 n.3.

[7] For example, Mr. Kushner refers to the fact that the digital revolution has facilitated the "unbundling" of albums, meaning consumers can buy only certain desired tracks rather than having to purchase an entire album just for one or two songs, as in the past. Kushner WDT, pp. 5-6 ¶ 12.

More importantly, Music Choice is not a "streaming" service, and launched its service over a decade before the actual streaming services entered the market in any material way; thus, it is disingenuous and misleading to include Music Choice in that definition. As I explained in my direct testimony, Music Choice began offering its service in the late 1980s and launched nationwide as a stand-alone entity in 1991. By the late 1990s, the PSS had obtained significant national market penetration and together had almost 20 million subscribers by 1999, of which Music Choice had almost 10 million.[8] During this entire period of the 1990s, record industry sales significantly increased and the record companies continued to post record-breaking revenues—topping out at well over $20 billion (in inflation-adjusted 2015 dollars) in 1999, according to RIAA. *See* Ex. MC 49, p. 4 ("U.S. Recorded Music Revenues By Format," https://www.riaa.com/u-s-sales-database (retrieved Jan. 17, 2017)).

Mr. Kushner's claim that the advent of streaming services in the late 1990s and early 2000s actually caused the recording industry's substantial revenue decreases starting in 2000 is unsupported by any empirical evidence. But if his unsupported claim were to be credited, then surely it would follow that part of the massive increase in record industry revenues for the first decade after the launch of the PSS was due to the promotional impact of the PSS.

[8] Even back in the late 1990s, Music Choice had far more subscribers than any streaming service had during the period coinciding with the initial record industry revenue decline identified by Mr. Kushner.

SoundExchange's Proposed Changes to the PSS Regulations Are Unsupported by Any Evidence, Would Be Unfair to Music Choice, and Should Be Rejected

SoundExchange and the PSS have operated under the existing regulations for decades without any evidence of a problem caused by the current language and structure of the regulations. After two decades, any changes to the regulations should require a showing of need by the proponent. SoundExchange has made no such showing. Instead, SoundExchange has clearly selected its proposed changes to benefit itself without any regard for objectivity or fairness. Any changes to the regulations after all this time would cause at the very least extreme inconvenience to Music Choice and would introduce new uncertainties that could lead to wasteful disputes and litigation. Moreover, many of the proposed changes would eliminate rights and protections Music Choice presently has.

Although it characterizes its proposed changes as a mere harmonization of the regulations with those for other licenses, with "certain conforming and editorial changes," SoundExchange's proposed regulations are actually drastically different from the current Part 382—so much so that it is a complex and time consuming task to even identify the current subsection analogous to each proposed subsection, or to determine that there is currently no analogous provision. This is due in large part to the fact that SoundExchange proposes changing the order of the topical subsections for no apparent reason. And, as SoundExchange has not provided a redline of the proposed regulations against the current regulations, it is very difficult to determine the correlation of proposed clauses to those currently in force.

However, despite the fact that SoundExchange has described its changes as "conforming" the PSS regulations with other regulations, it notably wants to keep the regulations different from the various other statutory license regulations with respect to the provision determining which party would bear the cost of an audit, because the PSS regulations are more favorable to SoundExchange on that point. This alone shows that SoundExchange is cherry-picking its changes and that its primary interest is gaining advantage rather than conforming the regulations.

In SDARS II, SoundExchange attempted the same gambit, seeking to make a large number of substantive (and less-substantive) changes to the PSS regulations, supposedly in the interest of "streamlining" and "conforming" those regulations. In that proceeding, the Judges overwhelmingly rejected SoundExchange's proposed regulations, except in rare instances where SoundExchange was able to provide specific evidentiary justification for the requested change. The Judges had good reason to refuse to make changes that were not specifically supported by evidence of need. The PSS regulations have been in place longer than those for any other Section 114 licensees, as they were created through the very first CARP proceeding. In this regard, Mr. Bender's claims that the PSS regulations "have tended to track the webcasting regulations" (Bender WDT, p. 33) is completely false. The PSS regulations were in place before the webcasting regulations. Moreover, none of the PSS operate webcasting services, so his claim that it is to licensees' benefit to conform the two is also patently false. With this in mind, and recognizing that there is no need to introduce new uncertainties into a well-established regulatory regime,

Music Choice has consistently declined to propose changes to regulations which have operated without issue for so long.

Particularly after the Judges' ruling in SDARS II, SoundExchange's failure to even specifically identify for the Judges (and Music Choice) all of the specific changes its proposed regulations would make to the existing PSS regulations, combined with its complete failure to provide any evidence supporting a need for those changes, should be sufficient for the Judges to reject SoundExchange's proposed regulations in total. Amazingly, hidden within SoundExchange's proposal are some of the exact same changes, such as changes to the auditing and confidentiality provisions of the PSS regulations, that the Judges rejected in the SDARS II proceeding. Yet SoundExchange *again* failed to provide any justification for those changes. If SoundExchange could not be bothered to specifically identify and support each of its changes, it is unfair to require Music Choice to comprehensively identify those changes and explain why each of them would prejudice Music Choice. Nonetheless, the specific proposed changes Music Choice was able to identify and that would most adversely impact Music Choice (addressed by category) include:

Proposed Changes That Would Improperly Limit the Scope of the PSS License

A number of the changes SoundExchange proposes would, taken together, significant limit the scope of the PSS license, contrary to the statutory intent underlying that license. The scope of the PSS license is determined by statute. Almost every year for at least the past decade, the recording industry has asked

Congress to alter, in one way or another, the scope or existence of the PSS license. In some instances, they have even succeeded in getting proposed legislation introduced. But every time, Congress has ultimately rejected those requests. SoundExchange should not be allowed to obtain substantive changes to the scope of the PSS license through administrative fiat. Examples of SoundExchange's proposed changes that would improperly limit the PSS license include:

1. *SoundExchange's proposed definitions of "Provider" and "Television Service"*

The terms "provider" and "television service" are not currently defined in the PSS Regulations. SoundExchange has proposed adding these defined terms, as follows:

> ***Provider*** *means a "multichannel video programming distributor" as that term is defined in 47 CFR §76.1000(e); notwithstanding such definition, for purposes of this subpart, a Provider shall include only a distributor of programming to televisions, such as a cable or satellite television provider.*
>
> *A* ***Televisions Service*** *is a noninteractive (consistent with the definition of "interactive service" in 17 U.S.C. 114(j)(7)) audio-only subscription service (including accompanying information and graphics related to the audio) that is transmitted to residential subscribers of a television service through a Provider which is marketed as and is in fact primarily a video service where*
>
> > *(1) Subscribers do not pay a separate fee for audio channels.*
> > *(2) The audio channels are delivered by digital audio transmissions through a technology that is incapable of tracking the individual sound recordings received by any particular consumer.*
> >
> > *(3) However, paragraph (2) above shall not apply to the Licensee's current contracts with Providers that are in effect as of the effective date of this subpart if such Providers become capable in the future of tracking the individual sound recordings received by any particular consumer, provided that the audio channels continued to be delivered to Subscribers by digital audio transmissions and the Licensee remains incapable of tracking individual sound recordings received by any particular consumer.*

Proposed § 382.10, App'x A at 9.

SoundExchange attempts to add these new definitions to the PSS regulations to support its proposal that Music Choice be required to pay new, additional royalties for any of its transmissions made through the internet. As noted above, that proposal should be rejected for many reasons, and for those same reasons these changes to the regulations should be rejected. But these changes should be rejected for another reason: they would drastically limit the scope of the PSS license, by making the PSS rate applicable only to Music Choice's service when it is provided to MVPDs via television. As I explain above, the Copyright Act does not limit the PSS license to a television platform, but allows the PSS to expand into other transmission platforms. Nor does the statutory license in any way limit the types of affiliates Music Choice provides its service to. These proposed changes would damage Music Choice by narrowing the scope of its rights under the PSS license—a license that was intentionally made broad by Congress, which contemplated and included various forms and media of transmissions through a PSS service in that license and upon which Music Choice has relied to transmit its service for decades. Nor has SoundExchange submitted any testimony or other evidence supporting why these radical changes would be appropriate. They should be rejected.

2. SoundExchange's proposed definition of "Licensee"

SoundExchange proposes changing the definition of licensee (currently in § 382.2) from "any preexisting subscription service as defined in 17 U.S.C. 114(j)(11)" to "*the provider of an SDARS or Preexisting Subscription Service that has*

obtained a license under 17 U.S.C. 112(e) or 114 to transmit eligible sound recordings." Proposed § 382.7, App'x A at 8. SoundExchange has explained the general purpose of this change—to "reflect types of services at issue in this proceeding"—but has made no attempt to explain why this change is necessary. *Id.* It is not. The services at issue in this proceeding comprise a closed group of existing licensees who have held licenses for many years. By express statutory language, this licensee group is not subject to expansion or to new entrants. There is no debate as to which entities and which branches of their services are at issue in this proceeding. This proposal serves only to add a new and unnecessary regulation which could muddy the waters of a regulatory scheme that has operated without issue on this point for decades.

3. Sound Exchange's proposed regulations regarding ephemeral recordings - current subsection § 382.3 (a) and (c); proposed subsection § 382.11(c)

The current subsection 382.3(a) provides that the fees payable under this license shall relate to "the making of any number of Ephemeral Recordings to facilitate such performances." SoundExchange has—without bringing this to the Judges' attention—proposed adding the qualifiers "necessary and commercially reasonable" to the phrase providing that any number of Ephemeral Recordings are included in the 5% payable under 17 U.S.C. §112(e) to its proposed § 382.1(c). This contrasts to the current regulations, which have no such additional "necessary and commercially reasonable" limitation.

While I cannot testify with certainty to the motive behind this change, as SoundExchange has provided no explanation, there may be situations in which it

would advantage SoundExchange to take the position that some ephemeral copies are not included under the PSS license, based on whether it deemed certain copies "necessary" or "commercially reasonable." Even if this were not the motivation for this proposal, SoundExchange's proposed language is vague and could open the door to disputes amongst the parties. In the over twenty years that Music Choice has been operating under the statutory license, there has never once been a dispute regarding ephemeral copies under the clear, existing regulation. As this change has been neither explained nor justified, the judges should reject it.

4. SoundExchange's proposed "scope" of Part 382

SoundExchange proposes adding a preamble to subsection § 382.1(a) to identify it as the subsection setting out the scope of Part 382—despite the fact that it has identified no instance in which the parties bound by this Part have been confused as to its scope. SoundExchange then narrows the language of this provision to apply to "public performance of sound recordings in certain Digital Audio Transmissions by *certain* Licensees." (Emphasis added). This language differs from the broad language of the current regulations, which state that the subpart "establishes rates and terms of royalty payments for the public performance of sound recording by nonexempt preexisting subscription services."

SoundExchange explains this narrowing change by stating that it "[u]sed defined term Digital Audio Transmission" but neglects to point out that it has also used another new defined term, "Licensee." It has also failed to address why, given that its proposed definition of Licensees is narrower than the current statutory

definition, the regulation should be further narrowed by the addition of the qualifier "certain Licensees." And these added words could damage Music Choice if SoundExchange were to argue that any branch of the Music Choice residential service did not fall under the "certain Licensees" proposed.

SoundExchange has provided no reason for why the current regulations are ineffective or need to be changed on this point. And, when read in conjunction with the proposed definitions of "Digital Audio Transmissions" and "Licensee", this proposed change only opens the door to differing interpretation, as it refers to "certain" Licensees in a context in which the licensees are a clearly defined group of already existing PSS and SDARS licensees.

Minimum Fee

SoundExchange proposes separating the existing language of the minimum fee provision—currently § 382.3(b)—into two subsections in separate areas of the Part—proposed subsections § 382.11 and § 382.2(c).

As an initial matter, the currently codified provision regarding the minimum fee appears to contain an error. The minimum fee regulation was one of the few issues resolved by settlement among the participants in SDARS II. That settlement, which SoundExchange agreed to, provided that the advance, minimum payments would be credited towards each licensee's *combined* Section 114 and 112 royalty obligations. This makes sense, because licensees make only one payment for the combined license, with a very small portion of that payment deemed attributable to the Section 112 royalty. When the parties submitted their stipulation regarding the

settlement to the Judges for approval, it expressly provided that the minimum payment would be credited to Section 114 as well as Section 112. *See Stipulation of SoundExchange Inc., Sirius XM Radio Inc. and Music Choice Regarding the Royalty and Minimum Fee Payable for the Making of Ephemeral Recordings*, Docket No. 2011-1 CRB PSS/Satellite II, May 25, 2012, attached as Exhibit MC 50. When the final regulations were issued by the Judges, however, the reference to Section 114 was left out. The absence of any mention of Section 114 in the currently codified minimum fee provision appears to have been a typographical error or clerical oversight, as it was not explained by the Judges in their Final Determination implementing the settlement.

Only allowing licensees to apply the minimum fee payment towards their Section 112 royalty obligations makes no sense, and is unfair to licensees. It makes no sense because the PSS are subject to one, combined, royalty obligation each month. It is unfair because if the substantial, $100,000 advance is applied only to the small portion of the monthly fee attributable to Section 112, it would take much longer for licensees to recoup their advance payment (and a smaller PSS like Muzak might not recoup the payment at all, even if it made overall royalty payments far exceeding the advance). SoundExchange has made no showing of why it should get the time value of that advance payment, or even why the advance is needed anymore. Indeed, Mr. Bender admits in his testimony that the minimum payment provisions related to the PSS are not really needed or viewed as important by SoundExchange because the actual royalties paid by the PSS are more than

sufficient to cover their relative share of SoundExchange's administrative expenses, unlike certain other statutory licensees. For these reasons, Music Choice asks the Judges to amend the regulation to clarify that the minimum payment is creditable to the entire statutory royalty obligation for the PSS, including Sections 114 and 112.

Aside from taking advantage of the apparent scrivener's error by incorporating the error into its proposed regulations, Sound Exchange has proposed separating the definition, of and requirements for payments toward, the minimum fee into two distinct subsections in different areas of the Proposed Regulations. These subsections refer to "minimum fee" in one location, and "minimum payments" in another, making it unclear whether these two provisions actually refer to the same issue. And SoundExchange once again has not provided any reason why it is necessary to change the format and location of a provision that has always operated as a single subsection within the regulations and split it into two separate subsections several sections apart. Given that this change, which is not supported by any rationale or evidence, could cause uncertainty and disagreements amongst the parties, the Judges should decline to adopt it.

Confidential Information

1. Confidential information generally – proposed § 382.5

The existing provisions governing confidentiality and the treatment of confidential information have been in effect for decades. Even though SoundExchange has not identified a single instance in which the current

regulations caused any problem that would justify changes to the regulations, its proposed regulations contain a sweeping overhaul of the existing regulatory language regarding confidential information, one that would deprives licensees the ability to adequately protect sensitive and confidential commercial information.

In its proposed § 382.5(a), SoundExchange present a significantly narrower definition of "Confidential Information," stating that it *means* the statements of account (whereas the existing definition states that confidential information shall *include* the statements of account as well as any other information designated as confidential in a confidentiality agreement). SoundExchange also proposes the new qualifier that confidential information is that which is "reasonably designated" as confidential. SoundExchange has not highlighted these narrowing changes for the Judges, nor has it presented any reasons why these changes are necessary. And these changes would be detrimental to the licensees, creating potential disputes as to whether information is "reasonably" designated as confidential, and possibly allowing SoundExchange to unilaterally deem information not "reasonably" designated confidential, and then share that information with impunity.

In addition, the final sentence of SoundExchange's proposed subsection (a) is made up of entirely new language, which states that "[t]he party seeking information from the Collective based on a claim that the information sought is a matter of public knowledge shall have the burden of proving to the Collective that the requested information is in the public domain." This denies the licensee owning

the information the ability to take part in the determination of whether that information is confidential.

Adopting this language would be extremely damaging to Music Choice. SoundExchange and its members should not be allowed to unilaterally (or collusively) determine whether Music Choice's information is confidential, as that power could provide it or its members a significant commercial advantage, to Music Choice's disadvantage. Music Choice regularly negotiates licenses and other agreements with the record labels and individual artists, and if employees or representatives of the record labels or artists were allowed to obtain Music Choice's confidential business information, it could be used to Music Choice's disadvantage in business dealings unrelated to the PSS license. Moreover, this would create an uneven playing field, where Music Choice would not have reciprocal access to the record companies' confidential business and financial information.

In the previous proceeding, the Judges rejected changes to the confidentiality provisions, noting Music Choice's concerns that implementing those changes could cause its confidential information to be provided to counterparties and result in exactly the same sort of commercial disadvantages I have just discussed. *Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services,* Docket No. 2011-1 CRB PSS/Satellite II, 78 Fed. Reg. 23,054, 23,074 (Apr. 17, 2013). As the changes SoundExchange now proposes are detrimental to Music Choice in many of the same ways, and as

SoundExchange has not justified (or even identified) these changes, they should not be adopted.

2. Treatment of confidential information - current § 382.5 (b) and (c); proposed § 382.5 (b)-(d)

SoundExchange's proposed § 382.5(c)(1)-(4) (addressing the treatment of confidential information) contain several major material changes that would substantially prejudice Music Choice. Generally, SoundExchange proposes less stringent terms for its duty to safeguard confidential information. And it has provided little explanation for these changes. While the current subsection § 382.5(b) provides that access to confidential information "shall be subject to an appropriate confidentiality agreement" and restricted to certain limited sets of individuals generally employed by or affiliated with SoundExchange, the analogous proposed subsection § 382.5(c) contains no mention of any confidentiality agreement. There is no appreciable burden to SoundExchange in requiring that its disclosure of licensees' confidential information be subject to a confidentiality agreement, especially when that minor burden is weighted against the damage that disclosure might otherwise cause.

SoundExchange also proposes expanding the scope of who may be granted access to the confidential information, and for what purposes access may be granted. Its proposed § 382.5(c)(3)—a completely new regulation—provides for granting access to the confidential information to "[o]utside counsel who is authorized to act on behalf of the Collective with respect to other matters pertaining to the collection and distribution of royalty payments and who require access to the

Confidential Information for the purpose of performing their duties during the ordinary course of their work."

SoundExchange has explained that this is a "[n]ew provision added because the Judges in *Web IV* moved attorneys from paragraph (1) to paragraph (2) to avoid the need for written confidentiality agreements with outside counsel, but outside counsel may need access to confidential information for purposes other than verification." App'x A at 5. SoundExchange states that this change would allow counsel to access confidential information without a written confidentiality agreement "for purposes beyond royalty verification, if those purposes pertain to the collection and distribution or royalties." Proposed Rates and Terms at 8. SoundExchange has made no attempt to identify what other valid purposes it could be referring to in these two explanatory notes. Even if such valid purposes existed, Music Choice would be significantly prejudiced by the sharing of its confidential information with outside attorneys not subject to confidentiality agreements. Absent such an agreement, SoundExchange's outside counsel would only owe a duty of confidentiality to SoundExchange; it would owe no duty to Music Choice. Indeed, under certain circumstances, SoundExchange's attorney might feel that its fiduciary duty to SoundExchange required it to use Music Choice's confidential information to SoundExchange's benefit in the absence of any binding contractual duty of confidentiality to Music Choice. And there is no appreciable burden to SoundExchange in requiring that *all* disclosure of Music Choice's confidential information to SoundExchange's counsel be subject to a confidentiality agreement.

That is the way that the regulations have functioned for decades, and SoundExchange has not cited a single example of a problem.

As I mentioned above, the Judges previously rejected changes to the confidentiality provisions in light of Music Choice's concerns that implementing those changes could cause its information to be provided to its counterparties and competitors, disadvantaging Music Choice not only in negotiations related to the statutory licenses but broadly across many of its license negotiations. *Final Determination* at 23,074. The same rationale be applied here to reject these proposed changes.

Finally, SoundExchange also proposes the addition of another entirely new provision, proposed § 382.5(c)(5). This provision, which would allow the Collective to grant "[a]ttorneys and other authorized agents of parties to the proceedings under 17 U.S.C. 112 or 114, acting under an appropriate protective order" to access confidential information, is not necessary. Confidential documents have been produced in this proceeding and those previous, even though the current regulations do not explicitly provide for the production and sharing of such documents. And, as with many of the preceding sections, SoundExchange has not justified this proposed change.

Audits

1. Audits generally - current §§ 382.6 and 382.7; proposed § 382.6

SoundExchange proposes condensing the current provisions governing audits of statements of accounts and of payments—§ 382.6 and § 382.7—into a single

section addressing all audit and verification activity. However, SoundExchange has failed to disclose that the proposed changes go beyond simply conforming and consolidating these subsections. There are substantive changes as well, which SoundExchange has neither identified nor explained.

First, proposed subsection § 382.6(a) is much longer than either of the current subsections § 382.6(a) and § 382.7(a), with no explanation of, or justification for, the additional words. It appears that this subsection has incorporated the definition of "interested parties" currently found in subsections § 382.6(g) and § 382.7(g), subsuming that subsection within the proposed subsection (a). While this change may not be substantive, it is nonetheless needless. If there is no substantive change to the meaning of this section, there is no reason to displace regulatory language that has been in force for two decades. The remaining changes to the audit provisions are, however, much more substantive, and more damaging to Music Choice.

SoundExchange notes that its proposed subsection § 382.6(b) (governing the frequency of audits) has been "[r]evised for clarity, and specifically to use the defined term Licensee and address frequency of auditing of the Collective." SoundExchange further explains that this change is "intended to approximate the predecessor provisions of 37 C.F.R. § 3826(b), § 382.7(b), § 382.15(b) and § 382.16(b)." But since the proposed definition of Licensee is an unjustified material addition (which, as I explain above, is unnecessary and prejudicial), changes made for the sole purpose of accommodating that definition are also unjustified.

The proposed changes to the audit provisions would be prejudicial to Music Choice. Despite SoundExchange's assertion that it has changed this provision in the interest of clarity, it actually appears to have made the meaning of this subsection *less* clear, and for no apparent reason. The proposed language contains the vague terminology that the audit may relate to payments in the "prior three calendar years," without saying prior to *when*. This language is significantly less clear than the existing regulations, which state that the three year period for which audits may be performed is the three years prior to the year in which the audit is *conducted*. This is an important distinction, as under the regulations SoundExchange may provide notice of intent to audit during one calendar year, but conduct the audit in the subsequent year.

2. Notice of intent to audit - current §§ 382.6(c) and 382.7(c); proposed § 382.6(c)

The current PSS regulations provide that the notification of intent to audit "shall also be delivered at the same time [as the submission of a notice of intent to the Copyright Royalty Board] to the party to be audited." 37 C.F.R. § 382.7(c). SoundExchange notes that it proposes changing the word "deliver[ed]" in that language to "send", "because the timing of delivery is in the control of the courier, not the sender" and states that this change is "intended to approximate the concept of 'serve' in the predecessor provisions of 37 C.F.R. § 382.15(c) and § 382.16(c)." App'x A at 6.

However, SoundExchange has not addressed whether the requirement of actual delivery is in fact a material element of the current regulations that provides

protection to the PSS. I believe that it is. Given that the proposed regulations lessen the burden on the verifying party to fully notify the party being audited, this change is material, to the detriment of the PSS. And again, SoundExchange has not provided any evidence that the existing PSS regulation has ever posed a problem.

In addition, the language stating that "the verifying entity must file" a notice of intent imposes a new burden on any licensee that defensively audits its own records pursuant to the defensive audit provision discussed below. If this language is taken to its literal extreme, it means that each time a service commissions a defensive audit, that audit must be noticed in the Federal Register to be effective. This is a major substantial change, which SoundExchange has completely glossed over and has not even attempted to justify.

3. Audit verification procedure – current §§ 382.6(e) and 382.7(e); proposed § 382.6(d)

SoundExchange proposes significant changes and additions to the existing language governing audit procedure. Most notably, SoundExchange seeks to limit the licensees' ability provide defensive audits performed in the normal course of business in lieu of audits performed at SoundExchange's request.

The final portion of SoundExchange's proposed subsection § 382.6(d) adds a new qualifier to the use of defensive audits, limiting their sufficiency to satisfy a requested audit "to the information that is within the scope of the audit." This new language would serve only to provide SoundExchange an opportunity to debate whether the defensive audit was complete and covered all of the information that should be subject to the audit. The language is somewhat vague, but

SoundExchange might argue that it means that if an otherwise qualified, independent auditor conducted an audit or verification pursuant to acceptable standards, but used sampling as part of that process (a common auditing technique for voluminous data where only representative samples of the data is tested, and then any errors are extrapolated out to the entire data set), then that audit could not serve as a complete substitute for an audit noticed by SoundExchange. This would defeat the entire purpose of the defensive audit provision.

This addition of a limitation not present in the current regulations has also not been highlighted for the Judges, or justified. Nor could SoundExchange easily justify weakening the Services' right to defensive audits. This defensive audit right was added in the first CARP proceeding at the request of the PSS, and was approved by the CARP expressly to minimize the burden of external audits if the PSS were willing to take on the cost and responsibility of independent auditing on a voluntary basis. Music Choice has availed itself of this ability, and has expended significant resources in doing so. SoundExchange has not demonstrated why this protection should be eliminated, but it nonetheless proposes language that weakens the provision's protective nature. Notably, SoundExchange sought to make this same change in SDARS II, but the Judges rejected it.

SoundExchange also seeks to add entirely new language providing that only the auditor specified in a notice of intent may conduct an audit. The requirement that the auditor be identified in the notice would be inconsistent with, and undermine, the language granting a licensee the ability to perform a defensive audit

in the ordinary course of business. Under SoundExchange's proposed language, it is possible a defensive audit would no longer fully meet the requirements of the regulations because the independent auditor that had already done the defensive audit would not be the same auditor named by SoundExchange in its audit notice. As noted above, the current regulatory language providing parties the opportunity to defensively audit themselves has a longstanding and important history and purpose. This provision was created in the original CARP proceeding, to shield the PSS from the burden of intrusive, repetitive audits, while still providing protection to copyright owners. Specifically, the CARP panel agreed that "consistent with the principle of limiting unnecessary expense and disruption, that where a Service can provide an audit already performed in the ordinary course of business by an independent auditor, pursuant to the generally accepted auditing standards, such audit and underlying work papers should serve as an audit on behalf of all interested persons" and noted that "[t]his procedure would result in fair opportunity to audit for copyright owners, while reducing the burden and expense of auditing upon the Services." *Report of the Copyright Arbitration Royalty Panel*, No. 95-5 CARP DSTRA, Nov. 12, 1997, ¶ 194. A copy of the relevant pages of that report is submitted as Exhibit MC 51.

In reliance on the very language in the existing PSS regulations that resulted from the 1997 CARP report, Music Choice has invested significant time, effort and expense into commissioning audits in the normal course of its business—specifically to avail itself of this provision if necessary. Changing this provision would not only

unjustly eliminate legal protections Music Choice currently has has; it would also deny Music Choice the benefit of the routine audits in which it has invested heavily.

4. SoundExchange's proposed § 382.6(e) – access to third-party records in furtherance of audit

SoundExchange, through this entirely new proposed subsection, seeks to impose an additional impracticable burden on the PSS to obtain third-party records during an audit process. This is yet another change that SoundExchange sought in SDARS II, but the Judges rejected. Such a requirement would be incredibly burdensome, with a serious potential to adversely impact Music Choice's business relationships with affiliates and any other third parties from whom Music Choice would be required to obtain non-Music Choice records. Music Choice has no legal means by which to require its MVPD affiliates to provide their internal business records to Music Choice, and it should not have to antagonize them by seeking voluntary disclosure (a request I am confident they would refuse). In the past, we have faced strong resistance when we have tried to obtain any commitment from our affiliates to provide us with access to their business records. And SoundExchange has provided no reason why this change is necessary. Since there is no evidence that there is any shortcoming with the existing audit procedures, this additional burden should not be imposed on Music Choice.

5. Audit disputes - proposed § 382.6(g)

The language of proposed subsection § 382.6(g) denies the PSS licensees the ability to dispute the findings of an audit. This would deny Music Choice a right that has been available to us throughout the history of these regulations, and a

right that is typical of any audit—the right to challenge the findings of an improperly conducted audit. If—as was the case in SoundExchange's prior audit of Music Choice—the findings were unfairly calculated or otherwise incorrect, we apparently would not have any ability to challenge SoundExchange's audit report, and would be compelled to pay any amount the auditor claimed was underpaid, irrespective of how improper the findings were. This is yet another change that SoundExchange sought in SDARS II but which the Judges rejected, noting Music Choice's concerns about the fairness of the proposed provisions. We urge the Judges to do the same again here.

6. Cost of audit - current §§ 382.6(f) and 382.7(f); proposed § 382.6(h)

SoundExchange proposes that for both PSS and SDARS, if the auditor determines there was an underpayment of 5% or more, the licensee must pay the reasonable costs of the audit, plus the amount of underpayment.

First, SoundExchange's proposed provision once again implies that, if the auditor finds that there was an underpayment, the service may not challenge the auditor's finding and settle for any amount less than the full amount that the auditor deems the service has underpaid. There is no such language in the current regulations. To adopt this language would deny Music Choice the right to challenge the findings of an improperly conducted audit or to simply avoid the legal fees of an audit challenge by settling for some amount less than the stated underpayment.

SoundExchange generally addresses only the portion of this proposed regulation relating to the amount of underpayment that would trigger cost shifting

– failing to even note the language that would remove the licensees' ability to settle an audit or challenge its finding.

Moreover, SoundExchange tries to justify imposing a new, uniform 5% threshold by stating that the SDARS cost-shifting threshold should also be lowered to meet the 5% that currently applies only to the PSS. SoundExchange supports this proposition only by noting that even a 5% underpayment by Sirius XM dwarfs the cost of an audit. It makes no attempt to justify holding Music Choice, a small service with much lower royalty payments than Sirius XM, to such a low threshold that is inconsistent with the remaining statutory licenses.

If there were *any* justifiable change to this provision of the regulations, it would be increasing the threshold at which underpayment triggers shifting the cost to the audited PSS. Notably, although SoundExchange seeks to "conform" the PSS regulations with other regulations in various areas noted above where the change would prejudice Music Choice to SoundExchange's benefit, it seeks to keep the existing 5% underpayment threshold for shifting the audit fees to Music Choice.

Every other Section 114 and Section 112 licensee has a 10% threshold, including the webcasting, SDARS, BES, and CABSAT licensees, rendering the 5% threshold objectively unfair. *See* 37 C.F.R. §§ 380.6(h) (webcasting), 382.15(g), 382.16(g) (SDARS), 383.4(a) (CABSAT), 384.6(g), 384.7(g) (BES). To date, Music Choice has reluctantly accepted this deviation from the industry norm based on the principle that the longstanding PSS regulations should remain unchanged, and also because Music Choice has never triggered even the lower threshold. However, if the

Judges are inclined to make any other changes to the regulations governing Preexisting Subscription Services, then this provision should be changed as well, to conform with the other licensee regulations which have a 10% underpayment threshold for shifting the cost of an audit.

Changes Used to Transition from Revenue-based to Subscriber-Based Fee

1. Royalty fees - current § 382.3 and proposed § 381.11

The current regulations provide for calculating the PSS royalties based on a percentage of the PSS' monthly gross revenues. SoundExchange, through its proposed regulation change and its proposed rates, advocates entirely abandoning a revenue-based royalty calculation for one based on subscriber counts. The technical infeasibility of the proposed methodology of calculating subscriber counts aside (as discussed below), these changes are based in an untenable proposal to adopt rates created for subsequent, not-preexisting services, and apply them to the preexisting subscription services.

2. SoundExchange's proposed definition of "Gross Revenues"

SoundExchange has omitted "Gross Revenues" from the defined terms in its proposed regulations. While it has not explained or even identified this omission, it is apparent that this term has been deleted due to the proposed shift from a revenue-based rate to a subscriber-based royalty rate for the PSS. However, as I have previously explained, the proposed change in the rate structure is untenable under the 801(b) objectives. Because this drastic change to the very structure of the

PSS rates should be rejected, the current rate-calculation mechanism—the PSS's gross revenues—should not be deleted from the regulations.

3. SoundExchange's proposed definition of "Subscriber"

The term "subscriber" is not currently defined in the PSS Regulations. SoundExchange has proposed adding this defined term, as follows:

> ***Subscriber*** *means every residential subscriber to the underlying service of the Provider who receives Licensee's service in the United States for all or any part of a month.*

Proposed § 382.10, App'x A at 9. SoundExchange has, by way of explanation, noted that this is a "[n]ew definition based on the definition of Subscriber in 37 C.F.R. § 383.2(g). Omitted the proviso in that definition because it is not apparent that either PSS requires the accommodation made therein." *Id.* SoundExchange provides no further rationale for why this new definition is needed, or for its selective adoption of a definition from regulations applicable to a different license.

The "proviso" language that SoundExchange cut from the existing CABSAT regulation (current § 383.2(g)) while asking they be applied to the PSS reads "provided, however, that for any Licensee that is not able to track the number of subscribers on a per-day basis, 'Subscribers' shall be calculated based on the average of the number of subscribers on the last day of the preceding month and the last day of the applicable month, unless the Service is paid by the Provider based on end-of-month numbers, in which event 'Subscribers' shall be counted based on end-of-month data."

The omission of that key language from the CABSAT regulation is yet another example of SoundExchange cherry-picking its changes. SoundExchange is

incorporating only those that are to its benefit. Even if the Judges were to accept a subscriber-based rate structure (which Music Choice urges them not to), SoundExchange's proposed language is untenable. Music Choice does not get subscriber counts on a daily basis, nor are the subscriber counts tied to individual subscribers. Music Choice is provided with the aggregate number of subscribers at the start and the end of each month. [redacted] And the language of § 383.2 that SoundExchange has omitted from this definition is the very language that would be required to make it feasible for Music Choice to calculate subscribers for the purpose of royalty payments. Although the addition of this defined terms is unwarranted, if the Judges do decide to incorporate it into the regulations, they should do so in a manner that actually conforms this regulation to the analogous definition in § 383.2(g)—including the proviso language that SoundExchange has omitted to Music Choice's detriment.

Statements of Account and Retention of Records

1. Statement of account - current§ 382.4(c); proposed § 382.3

SoundExchange proposes adding the requirement that, if a licensee is a partnership, its statements of account and the accompanying attestation must be signed by a partner. This requirement would be burdensome for any licensee that is a partnership. But it would be effectively impossible for Music Choice, which is a partnership made up of corporate entities. There is no way that Music Choice can demand that its partners (which are separate companies) do anything. Moreover, those partners do not run the day to day business and would not have the

knowledge necessary to attest to the statements. Finally, there is a limited timeframe for Music Choice to submit its statements of account, and even if we could overcome the first two obstacles (which I am confident we cannot), we could never complete the process in a timely enough fashion. And SoundExchange has not given any reason why these changes should be necessary. There has never been an issue in the past with statements of account signed by our regular employees. SoundExchange has never raised any dispute regarding the existing statement of account procedures we follow, and SoundExchange has not explained for the Judges why the current procedures are inadequate. Because SoundExchange has not justified this change, and because it is substantial and unduly burdensome to Music Choice, it should be rejected.

2. Certification - proposed § 382.3(b)

SoundExchange proposes requiring an annual certification by the licensee's chief financial officer, attesting that the statement of account for that year represent a true and accurate determination of the royalties due. SoundExchange has not explained why it is necessary to impose this completely new obligation on the PSS. While attesting to the recordkeeping accuracy in each year should not be unduly burdensome, requiring a chief financial officer to review the relevant records and sign such an attestation does impose an unnecessary burden. Given that SoundExchange has shown no evidence that there have been inaccuracies in the royalty statements submitted in the past that would be remedied by its proposed additional requirement, this is a needless change. Because SoundExchange has not

even highlighted this addition for the judges, let alone justified it, it should be rejected.

3. Retention of records – current § 382.4(e); proposed § 382.4(c)

The current regulations provide for retention of payment records for a period of three years after the end of the period for which that payment is made. SoundExchange proposes changing this language to provide for a period of "not less than three calendar years." This arguably increases the licensees' record keeping obligations, but SoundExchange has made no attempt to explain why a potentially longer time period is necessary. It is not necessary, and in fact it could be prejudicial. This new language could lead to disagreement among the parties or uncertainty as to the interpretation of this regulation. As SoundExchange has not even highlighted this change for the Judges, let alone explained its necessity or pointed to any situation in which the current regulatory language has led to a failure to retain records for an appropriate amount of time, this change should not be adopted.

Organizational Changes

1. Location of definitions:

SoundExchange has proposed moving definitions from section 2 of Part 382 to sections 7 and 10. Generally, those in proposed section 7 correlate to existing definitions, whereas those in proposed section 10 are altogether new definitions.

This reorganization causes administrative and interpretive difficulty to readers who must pass through several sections containing defined terms before

reaching the definition of those terms. In addition, SoundExchange has proposed significant changes to the substance of the definitions themselves, including the deletion or addition of definitions. Many of these changes, as I discuss above, would adversely impact Music Choice by limiting the scope of the PSS license or otherwise denying Music Choice legal protections it has always had. Taken as a whole, the relocation, reorganization, and substantive changes to the definitions sections of the regulations are incredibly substantive and potentially incredibly damaging, and SoundExchange has made no showing of why those changes should be adopted.

Other Prejudicial Changes

1. Compliance - proposed § 382.1 (b)

SoundExchange proposes revising subsection § 382.1(b)—which currently states that "[u]pon compliance with 17 U.S.C. 114 and the terms and rates of this subpart, nonexempt preexisting subscription services may engage in the activities set forth in 17 U.S.C. 114(d)(2)"—to the vague language that "Licensees relying upon the statutory licenses set forth in 17 U.S.C. 112(e) and 114 must comply with the requirements of 17 U.S.C. 112(e) and 114, this part 382 and any other applicable regulations." SoundExchange states that this wordy change is intended "to reference compliance with the statutory provisions as well as the regulations, as does current 38 C.F.R. 381.1(b) and (c) and 382.10(b)." This justification—that the proposed change comports with an overall rewrite of the regulation to more closely match regulations for other licenses—does not address the reason why this change is needed, as there is no indication that the parties have ever disputed that

compliance with these regulations and relevant statutes is required, or how those regulations and statutes should be interpreted. If—as SoundExchange appears to represent—there is no substantive difference between the current regulation and the proposed regulation, then there is no need to displace the current language. If, however, SoundExchange does intend some different meaning in this proposed language, it has entirely failed to justify that change. In either instance, the current regulations should not be disturbed on this point.

GEO Group's Rate Proposal Makes No Sense and Should Be Rejected

I have reviewed and attempted to make sense of the Written Direct Statement filed by GEO Group, but the testimony of Mr. Johnson seem focused entirely on irrelevant policy arguments (many of which seem to conflate issues related to musical composition copyrights with those of sound recording copyrights or otherwise relate to matters not at issue with respect to the PSS license). GEO Group's rate proposal does not make any more sense than its testimony. First, GEO Group propose that Music Choice pay a "per-performance" rate that is actually expressed as a per-subscriber rate starting at $0.10 per subscriber in 2018 and increasing to $0.20 per subscriber in 2022. Next, GEO Group proposes an alternative percentage of revenue rate of 45%.

GEO Group does not explain how these rates were derived, nor does it provide any benchmark, model, or any other evidence supporting these rates. Nor does GEO Group even try to explain how these rates would be consistent with the Section 801(b) policy standard. GEO's rate proposal should be rejected for these

reasons alone. Moreover, these rates would constitute an even larger rate increase than that proposed by SoundExchange. GEO Group's per-subscriber rate would require Music Choice to pay [ ] Consequently, the impact I describe above from SoundExchange's proposed rates would be even worse if GEO Group's rates were adopted. Those rates could not possibly be considered reasonable under the Section 801(b) policy factors.

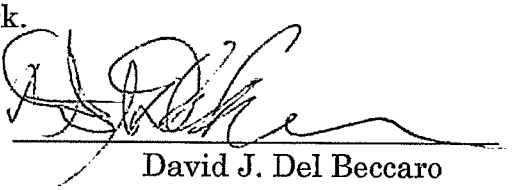
Although GEO Group's rate proposal is difficult to understand, it seems also to be proposing that Music Choice be required to offer a digital download service through which it would sell copies of sound recordings. There is nothing in the statutory licenses that could possibly allow for the Judges to impose such a requirement. Digital downloads are not subject to a compulsory license for sound recording rights. Music Choice therefore does not have the rights necessary to offer digital downloads, and has no desire to enter that completely different line of business. In the early days of the company, Music Choice provided retail sales of CDs in conjunction with its service (which, unlike operating a download service, did not require any license from the record companies). We abandoned that service because it was not profitable, and should not be required to re-enter the retail sales business in a way that would be even more unprofitable.

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Library of Congress
Washington, D.C.

In the Matter of: **Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)**	**Docket No. 16-CRB-0001-SR/PSSR (2018-2022)**

DECLARATION OF DAVID J. DEL BECCARO

I, David J. Del Beccaro, declare under penalty of perjury that the statements contained in my Written Rebuttal Testimony in the above-captioned matter are true and correct to the best of my knowledge, information, and belief. Executed this 16th day of February 2017 in New York, New York.



David J. Del Beccaro

WRITTEN REBUTTAL
TESTIMONY OF
DAMON WILLIAMS

PUBLIC VERSION

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
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In the Matter of: **Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)**	**Docket No. 16-CRB-0001-SR/PSSR** **(2018-2022)**

REBUTTAL TESTIMONY OF DAMON WILLIAMS

(On behalf of Music Choice)

My name is Damon Williams. I am the Senior Vice President of Programming Strategy and Partnerships for Music Choice. In my Written Direct Testimony, I explained the many ways in which the Music Choice residential audio service increases exposure and revenues for record companies and recording artists, including how exposure on the Music Choice service helps drive streaming traffic and record sales, and leads to the national distribution of more recordings. I also explained the lengths record companies go to in order to secure our help promoting their artists and records, from lobbying us for airplay to sending their most promising talent to our studios to give interviews, record performances, and promote their records through exclusive airings of new releases.

This lobbying activity is consistent across almost all the record labels we deal with, and we have been widely recognized by the entire record

industry as a very important promotional outlet for their music. This industry recognition is easily demonstrated by our inclusion on various Mediabase panels, as discussed in my Written Direct Testimony. Mediabase would not include us on those panels if the record companies did not recognize us as an important outlet. So I was surprised to read the Written Direct testimony of Michael Kushner, EVP of Business & Legal Affairs at Atlantic Records, who testified that "Atlantic has never viewed Music Choice as a major outlet for our music."

I was especially surprised by Mr. Kushner's testimony because I am well aware that Atlantic in fact heavily utilizes Music Choice as a promotional outlet, and devotes significant time, energy, and expense to seeking airplay and other promotional opportunities for its artists from Music Choice. Knowing many instances in which Atlantic representatives turned to us to help break a new single or push a trending single to the number one spot, it seems to me that the only reason Mr. Kushner would testify that Atlantic does not see us as a major promotional outlet is that he is not aware of what is actually going on outside the legal department at Atlantic. Whatever the source of his confusion, it is clear from the conduct of the Atlantic employees actually involved in the marketing and promotion of the company's artists that Atlantic views and treats Music Choice as an important outlet for its music.

Atlantic engages in all of the different types of record company conduct I described in my Written Direct Testimony, including lobbying us for airplay and asking us to allow their artists to visit Music Choice for promotional interviews and live performances. I note that in his testimony Mr. Kushner named five examples of current, important Atlantic artists: Twenty One Pilots, Paramore, Wiz Khalifa, and Slipknot. All five of these artists have visited Music Choice's studios or otherwise participated in Music Choice promotions. Even some of the specific examples I gave in my Written Direct Testimony involved Atlantic artists. For example, I talked about the role Music Choice played in pushing [[ ]] to the top of the charts. In that testimony, I mentioned Atlantic's efforts to lobby us to give the song more airplay, and the thanks they gave us for our important role in the song's success in the charts. But that is just one of the many instances in which we collaborated with Atlantic, at the label's request, to promote its artists.

Music Choice has a long history of working with Atlantic Records' artists and promotional teams. We began our strategic collaboration in 2006 following the launch of our VOD service in 2004. On VOD, and with coordinated cross-programming on our music channels, we helped to break some of Atlantic's emerging artists through feature placements on our "Fresh Crops" artist discovery program. We used the combination of music channel airplay and original content to build audiences for the emerging Atlantic

artists of the time. In the early years of our collaborative relationship with Atlantic, we featured several artists such as T.I., Flo Rida and Paramore, who have since gone on to become superstars.

Our relationship with Atlantic evolved further in 2008 or 2009, when [[ ]] stepped in to oversee rights negotiations with Music Choice. He did this because he recognized that airplay and promotions on our music channels and our then-emerging VOD channels could be incredibly valuable to the label. In fact, [[ ]] valued our promotion so much that he committed to providing T.I., then Atlantic's biggest hip hop star, to be featured on Music Choice as our artist of the month. In 2008 we also collaborated on a promotion for Atlantic artist (and now superstar) Flo Rida, and also featured Slipknot (a major artist on Roadrunner Records, which is distributed by Atlantic) as artist of the month during our Roctober promotion. A video from that Slipknot promotion is available at https://www.youtube.com/watch?v=IO4JKuVZAd8.

In the years since, we have consistently worked with Atlantic representatives to support their promotional efforts. In my Written Direct Testimony, I discussed the number of artist visits to the Music Choice studios in the years 2013 present, and submitted an exhibit listing the artists who visited us in each year. Looking back over that exhibit, I have found that many of the visits listed on that exhibit were by artists represented by Atlantic at the time. An updated version of that exhibit, with a new column

- [[ ]], who visited Music Choice on October 25, 2016. For this collaboration, we were approached by and worked with Atlantic Representatives [[ ]]. We captured original [[ ]] content for our programs Behind the Lines, Music Choice Now, Drops,[1] and Artist Portraits.
- [[ ]], who visited Music Choice on November 19, 2016. We worked with the artist and with Atlantic representative [[ ]] to record original content for Behind the Lines, MC Now, Drops and Artist Portraits. Emails from the artist's PR manager soliciting this collaboration are attached as Exhibit MC 55.
- [[ ]], who visited Music Choice on December 14, 2016. [[ ]], an Atlantic Representative reached out to us letting us know that [[ ]] and specifically asking us if we would be open to having him visit our studios. We collaborated with the artist and with [[ ]], to capture original content for Behind the Lines, MC Now, Did You Know, Artist

[1] A "drop" is an testimonial clip, usually featuring the artists themselves, used to increase awareness of an artist's content available on Music Choice (e.g. "Listen to my new single on Music Choice") or to promote the availability of that artist's Music Choice programming on a particular MVPD provider. Drops provide artists with valuable on-channel and off-channel promotion, increasing exposure to their music at Music Choice's cost.

Portraits, and Getty Photography. Emails regarding this studio visit are attached as Exhibit MC 56.

- [[ ]], who visited Music Choice on January 13, 2017. We worked with the artist and with Atlantic representatives [[ ]] to record two live performances and capture original content for MC Now, Drops, Artist Portraits, and for Getty Photography. For the performances we recorded, [redacted]]].
- [[ ]], who visited Music Choice on January 18, 2017. We collaborated with the artist and with Atlantic representatives [[ ]] to capture original content for MC Now, Hosted Playlist, Did You Know, Artist Portraits, and Getty Photography.
- [[ ]], who visited Music Choice on January 30, 2017. We collaborated with the artist and with Atlantic representatives [[ ]] to capture original content for MC Now, Hosted Playlist, Did You Know, Artist Portraits,

and Getty Photography. Emails relating to that studio visit are attached as Exhibit MC 57.

Music Choice coordinated airplay on our audio channels in conjunction with all of these promotions. In addition to taking advantage of our in-studio artist visits, Atlantic representatives engage in all the same lobbying activities seeking to get airplay on our audio channels as representatives from other labels.

One example of Atlantic representatives lobbying us for airplay is from April of 2014, when [[ ]]

In February of 2015, [[ ]] emailed Music Choice multiple times with lists of tracks for which he asked us to continue, increase or begin airplay. In June of that year, he reached out again, saying [["]] In August of 2015, he emailed once again Music Choice again, with four new singles for which Atlantic was either seeking new airplay or thanking us for current airplay and asking us to continue it. These emails are submitted as Exhibit MC 58.

But while some Atlantic reps email us for help (as in the examples above), generally the process by which Atlantic lobbies Music Choice for promotional exposure begins with a phone call. For years now [[ ]]

[redacted] have called us when they need to promote one of their top artists. [[redacted] January 2017 visit to Music Choice, which I discussed above, is a typical example of the process through which Atlantic and Music Choice collaborate. [[redacted]] called Music Choice asking for a meeting. The very next day, he came to our offices to let us know that [[redacted]]. [[redacted] offered to have [[redacted]] perform two acoustic songs at our studios, as well as give an interview, record original "drops", and cross-promote on his social media. [[redacted] did this because our Hit List and Pop Hits channels are widely popular with [[redacted]] fan base. And, as is the case with many such promotion solicitations from Atlantic, [redacted]] followed up with a conference call to go over the agenda for the visit.

And our promotional assistance does not go unmentioned. Atlantic representatives make it known that they need and appreciate our support. [[redacted]] have often expressed to us how thoroughly impressed they are by our execution and the professionalism of our staff. As I discussed in my Written Direct Testimony, Atlantic made it clear that our partnership with Atlantic to promote the 2016 single from [[redacted]] was a huge factor in the song's success. [[redacted]]. Emails from Atlantic regarding out role in the song's success are attached as Exhibit MC 59. And this is only one example of the many times Music Choice was instrumental in

helping an Atlantic artist climb the charts. Additional emails from Atlantic representatives lobbying us for airplay or thanking us for our help in promoting their artists and content are attached as Exhibit MC 60.

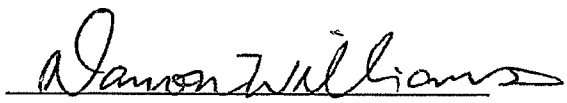
The fact that Atlantic dedicates its employees' time to lobbying Music Choice and provides its biggest stars—like superstar Bruno Mars, who just last year performed the Super Bowl halftime show—to Music Choice for in-studio promotions and interviews coordinated with audio channel airplay shows that the label does, in fact view Music Choice as a major promotional outlet. The amount of resources and opportunity cost that Atlantic must expend on all the promotional lobbying and collaboration activities I have described is *very* significant. It is, quite simply, impossible to reconcile that major investment with Kushner's obviously self-serving testimony regarding Music Choice.

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Library of Congress
Washington, D.C.

In the Matter of:	**Docket No. 16-CRB-0001-SR/PSSR (2018-2022)**
Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)	

DECLARATION OF DAMON WILLIAMS

I, Damon Williams, declare under penalty of perjury that the statements contained in my Written Rebuttal Testimony in the above-captioned matter are true and correct to the best of my knowledge, information, and belief. Executed this 16th day of February 2017 in New York, New York.



Damon Williams

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In re Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)	Docket No. 16-CRB-0001 SR/PSSR (2018-2022)

WRITTEN REBUTTAL TESTIMONY OF GREGORY S. CRAWFORD, PhD
(On behalf of Music Choice)

February 17, 2017

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I. Introduction

I.A. Summary of qualifications and experience

(1) I am Gregory S. Crawford, Professor of Applied Microeconomics at the University of Zurich in Switzerland. I received a PhD in economics from Stanford University in 1998. I was an assistant professor at Duke University, an assistant and later associate professor at the University of Arizona, and Professor of Economics at the University of Warwick in the United Kingdom. In 2007-08, I served as Chief Economist at the Federal Communications Commission (FCC), an independent federal regulatory agency charged with regulating a number of media and communications industries, including the broadcast and cable television industries. I reported directly to the Chairman of the FCC and advised him and his staff on a number of topics in these industries, including mergers, spectrum auction design, media ownership, network neutrality, and bundling. After my service at the FCC, I joined the Department of Economics at the University of Warwick as a full professor and, in 2013, moved to the University of Zurich as a (chaired) Professor of Applied Microeconomics. I am Director of Graduate Studies for the economics department. In 2011, I was invited to be a research fellow at the Centre for Economic Policy Research ("CEPR"), one of the leading European research networks in economics. In 2014, I was asked to be one of the (two) co-Program Directors for the CEPR's Industrial Organization Programme.

(2) I conduct research on topics in both industrial organization and law and economics. Much of my research has analyzed the cable and satellite television industries. I have published extensively at the intersection of these fields, evaluating conditions of demand and supply within the cable television industry and the consequences of regulation on economic outcomes in cable markets.[1] When the National Bureau of Economic Research (NBER) commissioned a volume analyzing the consequences of economic regulation across a number of American industries, I was asked to write the chapter on cable television.[2] I was also asked to write a chapter for the *Handbook of Media Economics* on the

[1] Gregory S. Crawford, "The Impact of the 1992 Cable Act on Household Demand and Welfare," *RAND Journal of Economics* 31, no. 3 (2000): 422–49; Gregory S. Crawford and Matthew Shum, "Monopoly Quality Degradation and Regulation in Cable Television," *Journal of Law and Economics* 50, no. 1 (Feb. 2007): 181–209; Gregory S. Crawford and Joseph Cullen, "Bundling, Product Choice, and Efficiency: Should Cable Television Networks Be Offered A La Carte?," *Information Economics and Policy* 19, no. 3–4 (Oct. 2007): 379–404; Gregory S. Crawford and Ali Yurukoglu, 2012. "The Welfare Effects of Bundling in Multichannel Television Markets," *American Economic Review*, 102(2): 643-85.

[2] The NBER is a private, nonprofit research organization dedicated to studying the science and empirics of economics. It is the largest economics research organization in the United States. The chapter is titled, "Cable Regulation in the Satellite Era," Chapter 5 in Rose, N., ed., "Economic Regulation and Its Reform: What Have We Learned?" forthcoming, University of Chicago Press.

economics of television and online video markets.[3] I have published numerous academic articles in such outlets as the *American Economic Review, Econometrica*, the *RAND Journal of Economics*, and the *Journal of Law and Economics*.

(3) I have testified twice previously before the Copyright Royalty Board ("CRB"), as a rebuttal witness for the Commercial Television Claimants in the matter of the distribution of copyright royalties for the distant importation of broadcast television signals in 2004 and 2005 and as a direct and rebuttal witness in the predecessor to this proceeding.[4] My *curriculum vitae* is submitted as Appendix G.

(4) I am being compensated for my time on this matter at a rate of $700 per hour.

I.B. Scope of charge and Summary of conclusions

(5) Counsel for Music Choice has asked me to evaluate the merits of the analysis and the evidence presented in the written direct testimonies of Dr. Paul Wazzan, Mr. Jonathan Orszag (as part of Dr. Wazzan's testimony), and Dr. George Ford submitted to the Copyright Royalty Judges on behalf of SoundExchange regarding the statutory royalty rate for digital performance rights in sound recordings for pre-existing subscription services ("PSSs") such as Music Choice. I also submitted my written direct testimony on Oct. 19, 2016 in this proceeding.[5]

(6) Dr. Wazzan uses a benchmarking approach to determine what he considers reasonable rates for sound recording performance rights for PSSs. He reviews what he considers the options for possible benchmarks, before concluding that the best available benchmarks are the per-subscriber rates charged for New Subscription Services (NSSs), also known as "CABSAT" rates. He also reviews the role the 801(b) policy factors should play in setting PSS rates, first agreeing with Mr. Orszag that setting marketplace rates is consistent with these policy factors and then considering whether differences in the benchmark market and his hypothetical "target" market require adjustments to account for the policy factors, concluding that they do not. He also addresses a number of side topics, including whether PSS providers should pay for Internet retransmission of their audio channels and whether Music Choice's existing contracts represent arms-length transactions between them and their cable distributor partners.

(7) It is my understanding that SoundExchange has proposed a monthly per-subscriber royalty for PSS of: $0.0190 in 2018; $0.0196 in 2019; $0.0202 in 2020; $0.0208 in 2021; and $0.0214 in 2022.[6]

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[3] Gregory S. Crawford, "The Economics of Television and Online Video Markets", Chapter 7 in *Handbook of Media Economics*, Volume 1, 2015, Pages 267–339.

[4] *See* In the Matter of Determination of and Terms for Preexisting Subscription and Satellite Digital Audio Radio Services, Docket No. 2011-1 CRB PSS/Satellite II.

[5] Written Direct Testimony of Gregory S. Crawford, PhD (Oct, 19, 2016). Hereinafter "Crawford WDT."

[6] *See* Written Direct Testimony of Paul Wazzan, ¶14. Hereinafter "Wazzan WDT."

These are equivalent to CABSAT rates during the years 2018–2020, with approximately 3% increases in each of 2021 and 2022.[7] Dr. Wazzan concludes that these rates "are a reasonable approximation of market royalties for the PSS and consistent with the 801(b)(1) objectives."[8]

(8) As an overview of my report, I conclude that the vast majority of Dr. Wazzan's and Dr. Ford's conclusions are simply incorrect. Dr. Wazzan's analysis and conclusion that CABSAT rates represent a useful benchmark for setting PSS sound recording performance rates is deeply flawed, as is his analysis of the 801(b) factors which form the basis for rate-setting in this proceeding. He draws further unjust conclusions in his support for a per-subscriber rate, his stated belief that Music Choice's cable company partners do not pay arm's-length rates for the Music Choice service, and that fees for Internet Transmissions to PSS Subscribers should not be included within the PSS rate. Dr. Ford's analysis has other problems. Despite nominally addressing whether PSS services substitute for or promote other sources of recording industry revenue, he provides no evidence in support of his arguments. By contrast, industry data, strategic documents, and behavior as well as a model of music discovery and consumption all strongly suggest promotional effects, with even modest such effects easily equaling the total PSS royalties that Music Choice pays to SoundExchange in a given year. The following paragraphs outline the broad arguments underlying each of these claims and point to the relevant sections of the report that address them in greater detail.

(9) In Section II, I describe in detail how Dr. Wazzan's conclusion that CABSAT rate represent a useful benchmark for PSS sounding recording performance rates is flawed. I begin in Section II.B by summarizing the alternative approaches taken by experts and the Copyright Royalty Judges (and its predecessors) in determining a reasonable PSS sound recording royalty rate, highlighting how Dr. Wazzan undertakes a benchmark analysis while my direct report conducted a model-based approach.

(10) Dr. Wazzan's proposed benchmark rates are those paid for sound recording performance rights in the CABSAT market. In Section II.C., I provide probative facts not considered by Dr. Wazzan regarding the history of the CABSAT rates, the firms active in this market, and relevant market outcomes for these firms. I conclude that Sirius XM is willing to pay very high CABSAT rates both because it perceives its limited CABSAT service as a promotional vehicle for its satellite radio service and because the expected costs of pursuing a CABSAT rate determination before the Copyright Royalty Judges very likely exceeded the expected benefits of such a proceeding. I also show that there has been no firm that has succeeded in profitably serving a wide portion of the cable audio market while paying CABSAT rates and that Stingray, the only firm paying CABSAT rates that actively competes for new business, is unlikely to break this trend.

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7 *See* Wazzan WDT, ¶14, ¶87.

8 Wazzan WDT, ¶89.

(11) In Section II.D, I finally dig into Dr. Wazzan's analysis. I show that CABSAT rates are an inappropriate benchmark for the hypothetical PSS market for at least four reasons: they do not fulfill Dr. Wazzan's own criteria as a benchmark, they are the product of a settlement in which SoundExchange is expressly prohibited from attempting to use the rates as a benchmark, they are not representative of a workably competitive marketplace rate, and there are many important differences in the cost and demand characteristics of CABSAT and PSS services. Furthermore, contrary to the principles of a benchmark analysis, Dr. Wazzan makes *no adjustments* to account for the many and manifest differences in cost, demand, and competitive conditions between the two markets.

(12) In Section II.E, I present an economic framework for evaluating Dr. Wazzan's proposal and show that if CABSAT rates were adopted in the PSS market, it would imply that *no PSS provider could offer a PSS service as a standalone business*. To show this, I demonstrate that existing CABSAT providers' net revenues,[9] an upper bound on their variable profits in the CABSAT market, are nowhere close to covering the fixed costs of a stand-alone PSS provider. I then show that even Music Choice could not profitably serve the PSS market paying CABSAT rates. I conclude by demonstrating that requiring a PSS provider to necessarily offer another service in order to have a profitable PSS service is contrary to the mandate in this proceeding, reduces competition, harms consumers, and imposes an outcome that would not be implementable in the absence of the proceeding. In Section II.F, I describe that Dr. Wazzan's conclusion that (unadjusted) CABSAT rates are a suitable benchmark is even more inappropriate when considering that 801(b) factors were put into place to protect PSS providers and that the upper bound of 801(b) rates should be no higher than market rates.

(13) In Section III, I show that Dr. Wazzan's analysis and adjustment of the 801(b) factors is equally flawed. Dr. Wazzan relies on Mr. Jonathan Orszag's opinion that market-based rates are inherently consistent with 801(b) factors one through three. In Section III.A., I show that these conclusions are incorrect as previous rate-setting bodies and the Courts have established that marketplace rate do not *necessarily* incorporate the 801(b) factors. I also describe in some detail that, as a matter of economics, marketplace rates do not generally satisfy the 801(b) factors as they will not generally maximize the availability of creative works to the public, they may not necessarily be fair, and they do not necessarily reflect the relative contribution of owners and users of sound recording performance rights. In Sections III.B and III.C, I show how Dr. Wazzan's understanding of the role of the 801(b) policy factors in a benchmark analysis is erroneous and that his specific arguments regarding the factors for the PSS market are also incorrect. I close, in Section III.D, by showing that SoundExchange' proposed rates are, of themselves, contrary to each of the four 801(b) factors.

[9] I use the term "net revenue" to refer to a firm's revenue *minus* its royalty costs. The net revenue for CABSAT providers is their CABSAT revenue minus their CABSAT royalties. I do not have information about their PRO (musical works) royalties and, as a result, these royalties are not subtracted to arrive at a CABSAT provider's net revenue. For Music Choice, I do have information about musical works royalties and therefore their net revenue refers to their VOD-adjusted residential audio revenue minus PSS or CABSAT royalties (depending on the analysis) and PRO royalties.

(14) In Section IV, I address additional incorrect and unjust claims made by Dr. Wazzan. In Section IV.A, I describe that the percentage-of-revenue rate structure historically used for PSS royalties is superior to per-subscriber structure because it is flexible under different market conditions and would avoid significant administrative burdens. I also show that it should *not* necessarily increase over time. In Section IV.B., I show that Music Choice's cable company partners *do* pay arm's-length rates for the Music Choice service and that the pattern of Music Choice's rates with its cable partners is completely consistent with size discounts that are common in the industry. Finally, in Section IV.C, I show that the fees for Internet transmission of PSS audio channels must necessarily be part of the PSS rate. SoundExchange has long accepted that web distribution of PSS channels is part of the PSS rate, a conclusion which is further supported by additional legal and economic reasoning.

(15) In Section V, I turn my attention to rebutting Dr. Ford's analysis. I explain that Dr. Ford does not provide any evidence of cross-platform substitutability of non-interactive PSS services with other interactive services that pay higher royalties. Dr. Ford's conclusion that the Copyright Royalty Judges can ignore any proposed adjustment for relative promotion is therefore not supported by any theoretical or empirical evidence on his part. Dr. Ford's "evidence," such as it is, is easily rebutted by survey evidence from the Web IV proceeding that non-interactive services (such as Pandora and iHeart) are not close substitutes for interactive, on-demand services (such as Spotify) and that far more users would substitute away from non-interactive services to free services than to on-demand services. His other proffered evidence, from the testimony of industry executives and citations to the (materially different) situation in the Web IV proceeding, are equally unconvincing.

(16) In a perfect world, I would offer a detailed empirical analysis of the promotional effects of PSS services. Unfortunately, such an undertaking is difficult and I do not. In the absence of such an analysis, I turn to industry data, strategy documents, and behavior. *All* provide support for the conclusion that non-interactive services like those provided by PSS are complementary to record companies' primary source of industry revenue (digital download and interactive services). Consumer usage patterns show overlap between multiple music platforms (especially non-interactive and interactive services), indicating that different services serve different purposes for consumers and are thus likely to be complementary. Record companies' marketing and promotion expenditures in a market with inconsequential royalty payments like the PSS market *necessarily* supports the idea that these companies expect to realize incremental revenue *in other markets* from increased plays in the PSS market. Industry documents also bear this out, clearly articulating the belief that increased plays on non-interactive services lead to increased downloads and/or interactive subscriptions and usage. Finally, I present a model of music discovery and consumption that supports the argument that consumers view curated, "lean-back" services (broadcast radio, non-interactive webcasting, PSS cable radio) as vehicles for music discovery and interactive, "lean-in" services (CDs, downloads, and streaming) for music consumption, again encouraging a view of complementarity between such services. Finally, I show that even a small net promotional effect would generate royalties for record

labels equal to what they currently earn from Music Choice in the PSS market, indicating that a royalty that would arise in the hypothetical PSS market that accounted for these factors would be significantly lower than what would arise when considering the PSS market on its own.

(17) For all of these reasons, the Copyright Royalty Board should reject Dr. Wazzan's proposed CABSAT benchmark rate for determining a reasonable royalty for sound recording performance right in the PSS market. Furthermore, *if* they make any adjustments in a PSS rate, however determined, to account for promotion or substitution, the balance of evidence strongly favors a promotional effect and thus a *lowering* of a PSS rate relative to a rate that ignores such features. In the sections that follow, I describe these conclusions in detail and provide supporting facts and analysis.

II. Wazzan's conclusion that CABSAT rates represent a useful benchmark for setting PSS sound recording performance rates is deeply flawed

II.A. Overview

(18) I show in this section that Dr. Wazzan's conclusion that CABSAT rates represent a useful benchmark for setting PSS sound recording rates is deeply flawed. To provide context for my conclusions, in Section II.B below, I briefly summarize the alternative approaches taken by experts and the Copyright Royalty Judges (and its predecessors) in determining statutory royalty rates. In Section II.C below, I then provide some useful and probative facts, not considered by Dr. Wazzan, regarding how CABSAT rates have been determined, who currently pays them, and patterns of CABSAT outcomes.

(19) In Sections II.D-II.F, I then describe each of three deep flaws in Dr. Wazzan's approach. First, as he himself describes at great length, the goal of a benchmark analysis is to find a benchmark market offering rates that are as similar as possible to those that would arise in the target (PSS) market and then to make adjustments to these rates to account for any differences in the two markets. In Section II.D below, I show that he fails in both of these tasks. I show that since the CABSAT rates were the product of a series of litigation settlements, by Dr. Wazzan's own arguments, they are an inappropriate benchmark for PSS rates, a conclusion further supported by the language in the most recent CABSAT settlement itself. In fact, that settlement agreement expressly prohibits SoundExchange from seeking to rely on those rates as a benchmark in this proceeding. I also show that the CABSAT market differs in material ways from the hypothetical market for PSS sound recording rights in its conditions of demand, cost, competition, and responsiveness to regulation, features ignored by Dr. Wazzan, and that he fails to adjust for any of these many differences. This again would rule out its use as a benchmark for the PSS market.

(20) Second, in Section II.E below, I show that, if adopted, the CABSAT-based rates supported by Dr. Wazzan would imply that no PSS provider could offer a cable radio service as a standalone business. This would both limit competition and harm consumers as well as impose an outcome that would not be implementable in the absence of this rate proceeding.

(21) Finally, in Section II.F below, I show that a CABSAT rate would be even more inappropriate when accounting for the intent and content of the 801(b) policy factors.

II.B. A brief summary of approaches to setting PSS sound recording performance rates

(22) To better understand Dr. Wazzan's overall approach, it is useful to contrast what he would like to do with approaches used by previous experts, the Copyright Royalty Judges, and its predecessors. Surveying the record in previous PSS proceedings as well as other, related, proceedings before the Copyright Royalty Judges, there are three general approaches usually taken by parties to determine rates for sound recording performance rights.

(23) The first approach is perhaps the most common and is the benchmark approach. There are either two or three steps to a benchmark analysis. In the first step, one identifies a benchmark market that shares as many characteristics as possible to a hypothetical, workably competitive, market for the targeted sound recording performance rights.[10] There are many possible ways for markets to differ, but Dr. Wazzan particularly emphasizes that it is important to choose as a benchmark a market for which rates are determined in workably competitive marketplace negotiations, i.e. benchmark rates that are not affected by regulation.[11] I demonstrate in Section II.D.3 below that he fails in this task.

(24) In the second step of a benchmark analysis, one adjusts for all differences between the two markets. This is particularly necessary if the benchmark rate is a regulated rate. After adjusting for all such differences, the proposed benchmark would (ideally) approximate outcomes that would arise in a workably competitive hypothetical market for the rights being considered.

(25) Whether a third step of a benchmark analysis is needed depends on the rate standard. Under a willing buyer/willing seller rate standard, only these two adjustments are needed. Under the "reasonable" rate standard applicable in this proceeding, however, the Copyright Royalty Judges must also take into account whether the adjusted benchmark rates also satisfy the policy objectives contained in Section 801(b) of the Copyright Act.

(26) Benchmarking is not the only methodology that may be used to derive appropriate royalty rates, however. One alternative approach to setting a rate for sound recording performance rights is to use a model to determine what would be such a rate. Modeling is particularly appropriate in the absence of reliable benchmarks, and is a well-accepted methodology in economics. There are either one or two steps in such an approach. First, one specifies a model of what are the demand, cost, and competitive conditions in the hypothetical market under consideration and how they would interact to yield market outcomes. One then estimates the key inputs into that model to predict the rate that would arise in the hypothetical market. Whether a second step is needed again depends on the rate standard. If the rate standard is a willing buyer/willing seller standard, then only the first step is needed. If the

[10] I describe the features of an ideal benchmark in my direct report. Crawford WDT, ¶50.

[11] *See* Wazzan WDT, ¶41, ¶64.

rate standard is an 801(b) standard, then a second step must decide whether to adjust the hypothetical market rates estimated in the first step to achieve the 801(b) policy factors.

(27) A final possible approach to setting rates for sound recording performance rights can arise when there already is a rate in place in the current market and the Copyright Royalty Judges are not presented with any usable evidence from either a benchmark or model-based analysis. In this case, they can use the existing rate as a starting point and decide if any of the evidence presented suggests whether that rate should be increased or decreased.

(28) In my direct report, I conducted a model-based analysis.[12] This analysis was based on Music Choice's projected financial performance for the 2018–2022 period using actual data through August 2016 and forecast data through 2018.[13] As stated there, my estimate of the royalty rate that would arise in the hypothetical market for PSS sound recording performance rights is 3.5% of residential audio service revenues and certainly no higher than 5.6% of these revenues. By contrast, Dr. Wazzan in his direct report conducts a benchmark analysis, concluding that the (unadjusted) rates in the CABSAT market represent a usable benchmark for reasonable royalties for PSS sound recording performance rights. In the balance of the next three sections, I show why such a conclusion is deeply flawed. I begin in the next subsection by summarizing features of the CABSAT market that will be useful for my arguments.

II.C. The CABSAT market

(29) In his direct testimony, Dr. Wazzan concludes that the CABSAT market represents the most reliable benchmark for PSS sound recording performance rights. He did not, however, provide any information about how CABSAT rates have been set, about the firms that pay CABSAT rates, about the reasons these firms pay these rates, or the implications of CABSAT rate levels for these firms. I do so in this section.

II.C.1. A short history of CABSAT rates

(30) There have been three proceedings to establish rates and terms for New Subscription Services provided through cable and satellite television packages, what SoundExchange and Dr. Wazzan call CABSAT services. The first covered the period from the inception of the CABSAT market until 2010, the second covered the period 2011-2015, and the most recent covered the period from 2016-2020. In this proceeding, Dr. Wazzan supports the rate request by SoundExchange for PSS rates that

[12] Crawford WDT, ¶¶63-184.

[13] Given most of their revenues come from long-term contracts, I believe Music Choice's forecast performance for 2017 and 2018 is likely to be very accurate. For the 2018–2022 PSS-III rate period, my estimate of Music Choice's 2018 performance is the average of 2016-2018 performance, with estimates for 2019-2022 adjusted to increase by a 1.5% inflation factor. Crawford WDT, ¶120.

are equivalent to the CABSAT rates from 2018-2020, with approximately 3% increases from those rates for 2021 and 2022.[14]

(31) It is important to note that the Copyright Royalty Judges have made no official rulings on rates in the CABSAT market. Instead, in each of these proceedings, a settlement was reached between SoundExchange and a small number of participants and each of these settlements was then adopted by the Judges without substantive review (as required by the applicable statute). In the first proceeding, the Judges received petitions to participate from SoundExchange, Sirius, XM, and MTV, but all the parties reached "full agreement on all issues" before the rate-setting proceeding was finished.[15] The Judges adopted this settlement after there were no objections.

(32) In the second proceeding, SoundExchange, Royalty Logic (RLI), and Sirius XM petitioned to participate, but, early in the proceeding, the Judges received a joint motion from all the parties requesting a stay and two of the parties, SoundExchange and Sirius XM, reached a settlement. RLI, which has never operated a CABSAT service, joined the request for stay but was not a signatory to the settlement. The Judges adopted the "proposed rates and terms" after receiving "no comments or objections" from any of the parties.[16]

(33) In the third proceeding, SoundExchange, Music Reports, the National Music Publishers Association (NMPA), Spotify, and Sirius XM petitioned to participate. The Judges subsequently dismissed the petitions to participate of NMPA and Music Reports, and Spotify withdrew from the proceeding, leaving only SoundExchange and Sirius XM as participants. In June, 2015, after receiving no objections, the Judges adopted the rates and terms for 2016–2020 based on a "joint motion" from SoundExchange and Sirius XM to "adopt a settlement of royalty rates and terms" for CABSAT services.[17] The per-subscriber rates for the 2016-2020 period were determined, for stand-alone contracts, to be $0.0179 per subscriber in 2016, $0.0185 in 2017, $0.0190 in 2018, $0.0196 in 2019, and $0.0202 in 2020.

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[14] Wazzan WDT, ¶87.

[15] Library of Congress, Copyright Royalty Board, 37 CFR Part 383, *Docket No. 2005–5 CRB DTNSRA, Digital Performance Right in Sound Recordings and Ephemeral Recordings for a New Subscription Service, Final Rule.* 72 Fed. Reg. 72,253. 72,254 (Dec. 20, 2007), https://www.loc.gov/crb/fedreg/2007/72fr72253.pdf. Hereinafter "2005-CRB DTNSRA."

[16] Library of Congress, Copyright Royalty Board, 37 CFR Part 383, [Docket No. 2009–2 CRB New Subscription II], Digital Performance Right in Sound Recordings and Ephemeral Recordings for a New Subscription Service, Final Rule. 75 Fed. Reg. 14,074, 14,075 (March 24, 2010), http://www.loc.gov/crb/fedreg/2010/75fr14074.pdf. Hereinafter "2009-2 CRB New Subscription II."

[17] Library of Congress, Copyright Royalty Board, 37 CFR Part 383 [Docket No. 14–CRB–0002–NSR (2016– 2020)], Determination of Terms and Royalty Rates for Ephemeral Reproductions and Public Performance of Sound Recordings by a New Subscription Service. 80 Fed. Reg. 36,927, 36,927 (June 29, 2015), http://www.loc.gov/crb/fedreg/2015/80FR36927.pdf. Hereinafter "14–CRB–0002–NSR (2016– 2020)."

II.C.2. Firms recently active in the CABSAT market

II.C.2.a. Sirius XM, DMX, and Stingray

(34) There are three firms that paid CABSAT rates during the most recent period for which I was able to obtain revenue and royalty data: Sirius XM, DMX, and Stingray.[18] The first, Sirius XM, is primarily in the satellite radio business.[19] It also offers 70 + of its satellite radio music channels through its offerings to DISH network subscribers, for which it pays CABSAT royalties.[20] It does not offer a music video channel or VOD service. I understand that it does not actively seek new CABSAT business.[21] As they are the only CABSAT ratepayer who was party to the recent CABSAT settlement with SoundExchange that forms the basis of SoundExchange's rate proposal, I provide more information regarding the reasons for Sirius XM's participation in the CABSAT market – and their willingness to pay so high a sound recording performance royalty – in the next subsection.

(35) The second, DMX, is a subsidiary of Mood Media, a Canadian company that primarily provides in-store audio and video products.[22] Between 2010 and April 2014, DMX offered its SonicTap service to DirecTV's digital television subscribers, for which they paid CABSAT royalties. Effective May 2014, another of Mood Music's subsidiaries, Muzak, acquired the rights to provide audio services to DMX's previous customers, for which they paid royalties at the PSS rate. Neither DMX nor Muzak offered/offers a music video channel or VOD service as part of its DISH or DirecTV service.

(36) Similar to Sirius XM, neither Muzak nor DMX actively seeks new cable radio business. The reasons are straightforward. As discussed above, both Muzak's and DMX's (and their common parent, Mood Media's) primary line of business is commercial background music. Before DMX was bought by Mood Media in 2012, I understand that the two firms competed with each other for this business in the United States.[23] In order to provide commercial background music, firms require a satellite distribution platform and a distribution network from which commercial clients can obtain satellite dishes to receive the necessary satellite signal. Prior to the market entry of DirecTV (in 1994) and

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18 I was able to obtain revenue and royalty data for these firms for the years 2013-2015. [[ ]]

19 Sirius XM provides various "music, sports, entertainment, comedy, talk, news, traffic and weather channels, as well as infotainment services, in the United States on a subscription fee basis through [its] two proprietary satellite radio systems" (Sirius XM 2015 10-K, F-9).

20 *See* DISH Music, https://www.dish.com/music/; *See also* DISH, Sirius XM Music, Channel Guide, https://www.dish.com/downloads/channel-lineup/siriuschannelguide.pdf.

21 Rebuttal Testimony of David Del Beccaro, 3-4. Hereinafter Del Beccaro WRT.

22 Mood Media describes itself as a "leading global provider of in-store audio, visual and other forms of media and marketing solutions in North America and Europe to more than 500,000 commercial locations across a broad range of industries including retail, food retail, financial services and hospitality" (Mood 2015, MD&A, 2. http://us.moodmedia.com/wp-content/uploads/2016/05/Q4%202015%20Mood%20Media%20MDA%20FINAL.pdf)

23 The original competitors in this area were Muzak and AEI. DMX merged with AEI in 2001. For support for the description of the history of competition in this market in this and the next paragraph, *see* Del Beccaro WRT, 6-9.

DISH Network (in 1996), I understand that Muzak and AEI (DMX's predecessor) maintained their own satellite platforms and distribution networks. The entry of DirecTV and DISH, however, presented them with a cheaper alternative: contract with one of these direct broadcast satellite (television) providers for distribution of their commercial background music service and save on the costs of maintaining their own satellite platform and distribution network. And so both did. Muzak contracted with DISH Network in 1996 and DMX contracted with DirecTV in 2005, contracts that are still in place today.

(37) Critically, the terms underlying these agreements are driven by both firms' primary lines of business, the market for commercial background music. Both firms also provide a residential audio service bundled with the contract for satellite distribution of their commercial music services, but I understand that the rates DISH Network and DirecTV pay for these residential services are below-market rates in the context of a stand-alone residential service.[24] As a residential audio service is not the focus of either Muzak or DMX and each is able to satisfy their core need for satellite distribution with their existing DISH and DirecTV contracts, neither therefore actively competes in the cable radio market.

(38) The last, Stingray Digital Group Inc., is a Canadian company that primarily provides cable audio services in Canada.[25] Current Canadian regulations require that 35% of the musical selections on Stingray's Canadian-produced music channels are Canadian artists.[26] Furthermore, to serve the French-speaking portions of Canada, at least 25% of these Canadian-produced channels are required to have at least 65% of their musical selections devoted to French-language Popular music.[27]

(39) For the years for which such data are available, Stingray Music (Galaxie) has proven to very profitable in Canada. Table 1 below shows the profitability of Galaxie, the predecessor to Stingray Music, as reported by its then-part-owner, the Canadian Broadcasting Corporation (CBC).[28] For the

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[24] I understand that Music Choice believes that these deals are currently priced less than [[2 cents]] per subscriber per month, far less than the average rate Music Choice receives of [[5.6]] cents per subscriber per month. *See* Del Beccaro WRT, 8 and Music Choice's average audio rate per month per billed subscriber in 2016. ("Sub Rate Detail - BW V2"). Sirius XM's CABSAT statements show that it received [[redacted]] cents per subscriber per month during 2013-2015. (SoundX_000145768, SoundX_000145778, SoundX_000145782.)

[25] Stingray describes itself as the "leading B2B music products, services, and content provider operating on a global scale, reaching an estimated 400 million Pay-TV subscribers (or households) in 152 countries." (Stingray FY 2016 Annual Report, 8.)

[26] The conditions of Stingray's pay audio service for its current term, from Sept. 1, 2015 to August 31, 2020, states: "(1)" The licensee shall ensure that at least 35% of the musical selections broadcast each broadcast week on Canadian - produced pay audio channels, considered together, are Canadian." *See* Canadian Radio Television and Telecommunications Commission, Broadcasting Decision CRTC 2015-377, Stingray Digital Inc., Aug. 17, 2015. http://www.crtc.gc.ca/eng/archive/2015/2015-377.pdf.

[27] "The licensee shall ensure that at least 25% of all Canadian-produced pay audio channels (other than those consisting entirely of instrumental music or of music entirely in languages other than English or French) devote each broadcast week at least 65% of vocal music selections from content category 2 (Popular Music), as defined in the Radio Regulations, 1986, as amended from time to time, to musical selections in the French language." *Ibid.*

[28] Stingray acquired Galaxie (renamed to Stingray Music) from Canadian Broadcasting Corporation in 2009. Stingray

years 2002-2008, it shows profit margins between 40.7% and 47.3% and net profits of between 5.1m and 13.8m Canadian dollars (between $3.3 million and $11.3 million).[29]

Table 1: Galaxie: Incremental revenues and expenses (as of March 31, CAD)

Thousands of Canadian dollars	2002	2003	2004	2005	2006	2007	2008
Revenues	10,822	13,275	16,254	17,217	20,235	21,838	22,146
Expenses	4,924	5,645	6,694	6,644	6,717	7,702	13,115
Repayments to main service	775	130	-	-	64	364	18
Net	**5,123**	**7,500**	**9,560**	**10,573**	**13,454**	**13,772**	**9,013**
Net as % of revenues (calculated)	**47.3%**	**56.5%**	**58.8%**	**61.4%**	**66.5%**	**63.1%**	**40.7%**

Source: CBC Radio-Canada Annual Reports 2002-2008. Notes: (1) Galaxie is operated "under license conditions that require the reporting of incremental costs and revenues." (2) Repayments to main service include: "Capital expenditures for the acquisition of equipment to introduce, maintain and expand the Specialty Services are made by the Corporation from its capital appropriation with an approved corporate repayment plan for recovery from the Specialty Services' revenues. Those repayments are funded from the accumulated excess revenues over expenses." (3) CBC operates Galaxie "under license conditions that require the reporting of incremental costs and revenues. The expenses of the specialty services exclude long-term liabilities such as long-term employee future benefits liabilities that will be included in the results at the time the related benefits are paid by the specialty services. accordingly, these accruals are allocated to the other categories of expenses in the Consolidated statement of operations."

(40) Stingray offers a version of its music service in the United States under its "Stingray Music" brand, for which it pays CABSAT royalties.[30] It does not offer a linear music video channel in the United States and, until recently, did not offer a US VOD service.[31]

(41) Of the two firms that continue to pay CABSAT rates, only Stingray actively seeks out new business in the cable radio market. As discussed in greater detail in my direct testimony, it entered the US market in 2010 and succeeded in signing relatively small cable operators by undercutting Music Choice on price.[32] As also discussed there, Music Choice estimates that between 2012 and 2014, it was able to win contracts in competition with Stingray despite a [[ ]] price premium, due in large part to the fact that it provided video services when Stingray did not.

(42) In October 2014, Stingray signed its first big cable operator, AT&T. As I show in Table 3 below, because large operators pay relatively low per-subscriber fees, this has had a significant impact on the

Prospectus, May 2015, 22.

29 I used the average monthly exchange rate (USD per 1 Canadian dollar) for the years ending March 2002 and March 2006. These were $0.6387 and $0.8380. Federal Reserve Economic Data, https://fred.stlouisfed.org/series/DEXCAUS.

30 Naturally, none of the Canadian regulations requiring Canadian and French-language content apply to its US offerings.

31 Stingray offered its Concert TV VOD service for live concerts beginning in 2014. *See* Stingray News and Press Releases, "Stingray Digital Expands Concert TV services in the US," Aug 7, 2014, http://www.stingray.com/about-us/press-room/news-and-press-releases/stingray-digital-expands-concert-tv-services-us. It expanded this to include music videos in 2015. *See* Stingray News and Press Releases, "Stingray Expands Distribution Agreement with Comcast," May 2, 2016, http://www.stingray.com/about-us/press-room/news-and-press-releases/stingray-expands-distribution-agreement-comcast.

32 Crawford WDT, ¶147.

share of Stingray's CABSAT revenue that goes to sound recording performance royalties (increasing it from [[ ]] in 2015).[33]

II.C.2.b. Data patterns for firms serving the CABSAT market

(43) Several features of the CABSAT market will prove useful for my ultimate analysis and so I present them here. First, a key characteristic of each of the firms that pay CABSAT royalties is that they each earn a very small share of their company-wide revenue from the CABSAT market. Table 2 below shows, using publicly available data, the share of total revenue each of these firms receives from the CABSAT market. [[[34]]]

Table 2: CABSAT revenue as a percentage of total firm revenue

	Sirius XM	DMX	Stingray

Source: Sirius XM: Sirius XM 2015 10-K, F-4; SoundX_000145768, SoundX_000145778, SoundX_000145782; DMX: Bloomberg, SoundX_000145804, SoundX_000145801; and Stingray: Bloomberg, SoundX_000145790, SoundX_000145813, SoundX_000145808. Note: DMX 2014 figures are for January to April only.]]

(44) Table 3 below reports the share of CABSAT revenues each of these firms pays to SoundExchange in sound recording performance royalties. [[[35]]]

[33] Stingray's CABSAT's CABSAT statements show that in [[ ]] illustrates the impact of decline in revenue for the larger cable providers. (SoundX_000145813, SoundX_000145808.)

[34] *See* Section II.D.4 below for the share of revenue Music Choice earns from the PSS market.

[35] As explained further in the previous subsection, the [[ ]] Stingray's CABSAT statements show that its number of subscribers [[ ]] and its monthly CABSAT revenues [[ ]] (SoundX_000145813 and SoundX_000145808.)

Table 3: Percent of CABSAT revenues paid as sound recording royalties

	Sirius XM	DMX	Stingray
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

Sources: Sirius XM: SoundX_000145768, SoundX_000145778, SoundX_000145782; Stingray: SoundX_000145790, SoundX_000145813, SoundX_000145808; and DMX: SoundX_000145804, SoundX_000145801. Note: DMX 2014 figures are for January to April only.]]

II.C.3. Why is Sirius XM willing to pay so much in CABSAT royalties?

(45) As Table 3 clearly shows, Sirius XM paid CABSAT royalty rates of between [redacted]]] between 2013 and 2015, far higher than the current 8.5% PSS royalty rate. Recall from Section II.C.1 above that these royalty rates are the result of a settlement between Sirius XM and SoundExchange. Which invites the question: why is Sirius XM willing to pay so much in royalties?

(46) In my opinion, there are two reasons. First, both SoundExchange and Sirius XM have previously acknowledged the fact that *Sirius XM's CABSAT service is used as a promotional vehicle for its SDARS service*. In its findings of fact in SDARS I, SoundExchange wrote "XM and Sirius provide PSS-type audio music channels to satellite TV at a trivial or [redacted] price, because they view the PSS service as one that can promote increased use and subscribership of the SDARS services."[36]

(47) This view was supported by two of Sirius and XM's own experts as well as Sirius's CEO. Dr. Tasneem Chipty, when asked in her deposition in the first CABSAT proceeding, "In your testimony you discuss how Sirius and XM use these services primarily as a promotional device for their satellite radio services. Is it your testimony that XM and Sirius wouldn't have entered into these arrangements but for the promotional effect they hoped to achieve?", answered "That is my understanding, yes."[37] Similarly Dr. John Woodbury, when asked in his deposition in SDARS I, "[XM and Sirius] sell a [PSS-type] service to Echo Star and DISH for nothing. Right?", answered "I've heard it said that was the case, yes." He further elaborated, "my understanding is that the reason that's occurring is because XM and Sirius regard DirectTV and Echo Star [DISH Network] as fields for acquiring additional subscribers, that these are folks that are more likely to subscribe to XM and Sirius, as opposed to the general population. I'm not aware, for example, that XM and Sirius are competing to obtain access on cable systems, which is where Music Choice, I think, predominantly has most of its customers."[38] Similarly Sirius CEO Joseph P. Clayton, in a press release announcing the Sirius-DISH partnership,

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[36] Docket No. 2006-1 DSTRA, Proposed Findings of Fact of SoundExchange, Inc. ¶1309. https://www.loc.gov/crb/proceedings/2006-1/pff-cl-10-01-07-sx-pff-public.pdf.

[37] Docket No. 2006-1 DSTRA. Rebuttal Testimony of Janusz Ordover, FN4 citing SX Ex. 209 RP (Trial Testimony of Dr. Tasneem Chipty on behalf of XM and Sirius Radio. Docket No. 2005-5, Tuesday July 10, 2007, 166).

[38] Docket No. 2006-1 DSTRA, Woodbury testimony at 55, 58.

commented, "Once they hear what we [Sirius] have to offer, we believe that DISH Network customers will want to have SIRIUS in their cars, boats, RVs and trucks, as well as their homes."[39]

(48) Even Dr. Wazzan agrees that when making decisions in the CABSAT market, Sirius XM does so primarily due to considerations in the satellite radio business. When discussing Sirius XM's direct licenses, he concluded "[b]ecause Sirius XM's CABSAT business constitutes such a small part of Sirius XM's overall business, its direct licenses for sound recording rights covering its whole suite of service offerings cannot be understood as specifically reflecting the economics of the CABSAT service. If anything, they must overwhelmingly reflect the economics of the SDARS business."[40]

(49) That Sirius XM views its CABSAT business as a promotional vehicle for its satellite radio services has many implications, but the most obvious is that such a firm is clearly not making decisions that would be representative of outcomes in the hypothetical market for PSS sound recording performance rights. I revisit this point in Section II.D.3 below.

(50) The second reason for which I believe that Sirius XM was willing to agree to such a high royalty rate for CABSAT sound recording performance rights is that the expected costs of engaging in a CABSAT rate proceeding very likely exceed any potential expected benefits in terms of a lower rate.

(51) To show this, I began by calculating the net revenue for each of Sirius XM, DMX, and Stingray from their CABSAT services for the years 2013-2015. Net revenues are defined as each firm's CABSAT revenue less their CABSAT royalty costs. So calculated, these net revenues are a crude but conservative estimate of the maximal variable profits each firm could have achieved in the CABSAT market over those years. It is a conservative estimate of variable profits as it does not subtract any of the variable costs other than CABSAT royalties each firm must have paid, for example for musical works performance rights, nor does it subtract any of the fixed costs required to serve the CABSAT market.

(52) Table 4 below reports the net revenue for each of Sirius XM, DMX, and Stingray from their CABSAT services during the period 2013-2015.

[39] Sirius Press Release, "SIRIUS Satellite Radio Now Offered to Millions Of Dish Network Homes," May, 20, 2004. http://investor.siriusxm.com/investor-overview/press-releases/press-release-details/2004/SIRIUS-Satellite-Radio-Now-Offered-To-Millions-Of-Dish-Network-Homes/default.aspx#sthash.3vHG6gzy.dpuf.

[40] Wazzan WDT, ¶56.

Table 4: Net revenue (CABSAT revenue minus CABSAT royalty)

Thousands of dollars	Sirius XM	DMX	Stingray
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

Sources: Sirius XM: SoundX_000145768, SoundX_000145778, SoundX_000145782; Stingray: SoundX_000145790, SoundX_000145813, SoundX_000145808; and DMX: SoundX_000145804, SoundX_000145801.]]

(53) I focus for now only on the values for Sirius XM in this table. It shows that Sirius XM received net revenue of between [redacted]]] As shown in Table 3, these represent CABSAT royalty rates of between [[[redacted]]].

(54) To understand why they would be willing to pay such high rates, imagine that Sirius XM considered the costs and benefits of seeking lower rates via a CABSAT proceeding. The potential benefit would be a reduction in the royalty that they currently pay. How much they might expect to achieve is unclear. For them to achieve a material benefit, they would necessarily require a significant reduction in the CABSAT royalty rate. But this would be extremely uncertain: there has never been a decision in a CABSAT proceeding, and the per-subscriber rates that have been part of each of the three settlements between SoundExchange and CABSAT proceeding participants have consistently increased since their inception, something the Judges might consider as precedential in a rate proceeding.[41]

(55) While the benefits are uncertain, the costs are less so. The cost of litigating a proceeding before the Copyright Royalty Judges is expensive: Music Choice paid [redacted]]] in order to participate in the previous PSS proceeding and a CABSAT proceeding would likely cost Sirius XM at least a similar amount.[42] Spreading the cost of such a proceeding over five years implies incurring an assured cost of over [redacted] to try to increase the profitability of a line of business earning. From Table 4, (at most) $300,000-500,000/year. Faced with expected annual litigation costs that more than outweigh annual net revenues, it is not surprising that Sirius XM instead chose to settle.

(56) This is particularly true when one considers the overall importance of Sirius XM's CABSAT business relative to their overall operations. Table 2 above showed that Sirius XM's CABSAT revenues represent less than [[[redacted]]] of their total revenues. Litigating a rate settlement before the Copyright

[41] Per-subscriber CABSAT rates have increased by 169% for stand-alone contracts (from $0.0075 per subscriber from the inception of the market until 2006 to $0.0202 per subscriber in 2020) and by 52.7% for bundled contracts (from $0.0220 per subscriber from the inception of the market until 2006 to $0.0336 in 2020). Sirius XM paid CABSAT rates at the [[[redacted]]] during 2013-2015. *See* 2005-CRB DTNSRA, 2009-2 CRB New Subscription II, and 14-CRB-0002-NSR (2016-2020).

[42] Music Choice PSS-II rate proceeding legal expenses. *See also* Del Beccaro WRT, 4.

Royalty Board not only costs money, it costs time and attention. Sirius XM already faces quinquennial SDARS proceedings for which such time and attention is critical. Given the tiny share of their revenue that comes from the CABSAT market and the consequent lack of importance the CABSAT market likely has in their strategic decision-making, the *opportunity cost* of their time is likely to far exceed the direct financial costs. It is therefore no surprise that Sirius XM chose to reach a settlement with SoundExchange that provided SoundExchange with the lion's share of the benefit from Sirius XM's CABSAT service.

II.C.4. There has been no firm that has succeeded in serving a wide portion of the cable audio market while paying CABSAT rates

(57) As mentioned above, the only CABSAT provider that actively competes for business in the cable audio market while paying CABSAT rates is the Canadian company Stingray. It is a relatively new entrant, however, and it is not at all clear that it will be viable in the long run.

(58) History has not been kind to firms seeking to provide a cable audio service while paying CABSAT rates. As discussed above, Sirius XM has, since 2004, offered its audio channels on the DISH satellite provider, but does so for promotional reasons. Between 2007 and 2010, MTV tried to leverage its strong brand in music videos to offer a cable radio service, and indeed was a party to the first CABSAT settlement signed in 2007, before ultimately deciding to exit the business in 2010.[43] Furthermore, DMX entered but now has completely abandoned the CABSAT market, and, as discussed above, because both have contracts with satellite providers in order to secure distribution cost savings for their commercial background music products, neither DMX nor Muzak actively seeks new cable radio business, despite being able to pay the lower PSS rate.[44]

(59) Could Stingray succeed long-term in the US cable audio business paying CABSAT rates? Stingray does not report its overall financial performance by its lines of business, so it is not possible to know with certainty if its CABSAT business in the US is profitable paying these higher royalty costs. Furthermore, neither SoundExchange nor Dr. Wazzan has provided any evidence that it is or will be, or that any firm can profitably provide a cable radio service paying CABSAT rates. I understand that

[43] Rebuttal Testimony of David J. Del Beccaro, 18, Docket No. 2011-1 CRB PSS/Satellite II ("With respect to Urge, MTV entered the CABSAT market for only a short time, beginning in 2007. Although Urge was able to take away some of Music Choice's affiliates by undercutting our price and/or bundling the service along with MTV's popular video channels, the Urge cable radio channels were not as popular with subscribers as Music Choice's channels and MTV discontinued the Urge cable radio service in 2010. We have since regained many of the affiliates we had lost to Urge, and in all instances listening intensity increased substantially after Music Choice replaced Urge. Having left the market this way, it is doubtful that MTV would want or be able to re-enter, even if Music Choice went out of business.").

[44] The original DMX was a PSS rate-payer, but filed for bankruptcy and was liquidated. The company that purchased those assets was also called DMX but was required to pay CABSAT rates. Del Beccaro WDT, 44. Given that DMX's SonicTap service has since 2014 paid PSS rates, I assume there is some feature of the Mood Media corporate structure that allows them to license both firm's services at these (lower) rates.

after six years of attempting to gain market share by undercutting Music Choice's prices, Stingray has only been able to obtain one large affiliate and has only taken [redacted] of the MVPD market.[45]

(60) Given the information I have at my disposal, I conclude that it is unlikely that Stingray can succeed long-term in the US cable audio business paying CABSAT rates. As shown in Table 3 above, Stingray's share of total CABSAT revenue paid in royalties to SoundExchange jumped from a [redacted] since it signed AT&T in October 2014.[46] It would increase even more if it signed more large customers.

(61) High CABSAT royalty rates make it difficult to recover Stingray's fixed costs of serving the US CABSAT market. As I show in Table 5 in Section II.E.2 below, Stingray's net revenue, an upper bound on their variable profits from the CABSAT market, is less than [[redacted]] the value of Music Choice's fixed costs from serving the PSS market.[47] Because Stingray can subsidize its American operations from its Canadian and other non-CABSAT profits, it is possible Stingray has lower fixed costs of serving the US market than does Music Choice, but I find it unlikely that they would be [[redacted]] lower.[48] Furthermore, in order to be competitive with Music Choice, Stingray has begun offering a VOD service and must pay royalties not only for its CABSAT service, but also for this video service, and all from the (lower) bundled fees it earns from its cable affiliates.[49] I therefore conclude that it is very unlikely that Stingray is or will ever be profitable in the CABSAT market if they have to pay the existing (or broadly similar) CABSAT rates.

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45 Del Beccaro WRT, 9-11.

46 *See* Table 3: Percent of CABSAT revenues paid as sound recording royalties for details. Note also that the value of this client has since declined given AT&T's stated decision to de-emphasize its U-verse television service since its purchase of DirecTV in July 2015. *See* AT&T Inc., Form 8-K, January 25, 2017. https://www.att.com/Investor/Earnings/4q16/8k_4q16.pdf. ("During the fourth quarter of 2016,… U-verse subscribers declined 262,000 as we focused on profitability and increasingly emphasized satellite sales"); *see also* Scott Moritz, "AT&T Takes U-Turn on U-Verse as it Pushes Users Toward DirecTV," Bloomberg, Feb. 16, 2016, http://www.bloomberg.com/news/articles/2016-02-16/at-t-takes-u-turn-on-u-verse-as-it-pushes-users-toward-directv. This de-emphasis has indeed come to pass, with AT&T's U-verse subscribers declining by an extraordinary 27.3% (to 4.25 million from 5.85 million) in the five quarters between September 30, 2015 and December 31, 2016 (https://www.att.com/Investor/Earnings/4q16/master_4q16.pdf, https://www.att.com/Investor/Earnings/4q15/master_4q15.pdf). *See also* AT&T Press Release, "Stingray Music brings all good vibes to AT&T U-verse customers, Stingray Music App Launches on U-verse TV," Oct. 29, 2014, http://www.prnewswire.com/news-releases/stingray-music-brings-all-good-vibes-to-att-u-verse-customers-280769832 html.

47 Stingray's 2015 net revenue of [redacted] million is about [redacted] of the PSS fixed cost of [redacted] million.

48 And recall that net revenues are only an estimate of a firm's *maximal* variable profit from serving the CABSAT market. For example, it does not include the costs they must pay for their musical works performance rights. Thus [redacted] true variable profits from the CABSAT market in 2015 are necessarily even less than [redacted] of Music Choice's fixed costs.

49 Del Beccaro WRT, 10-11.

II.D. CABSAT rates are an inappropriate benchmark for the hypothetical PSS market

(62) Dr. Wazzan states repeatedly how there are few suitable benchmarks for the PSS market.[50] He first rejects all the benchmarks proposed by SoundExchange's expert witness in the previous proceeding, Dr. Ford.[51] After considering other alternative benchmarks, Dr. Wazzan dismisses them all and concludes that CABSAT rates established under 37 C.F.R. 383 (CABSAT rates) are the only available alternative.[52] This conclusion is faulty for no less than four reasons.

II.D.1. *By Dr. Wazzan's own arguments*, settlements should not be used as benchmarks

(63) In his direct report, Dr. Wazzan reviews the history of PSS rate-setting, emphasizing how in several proceedings the relevant authority set rates that were the result of settlements between SoundExchange and Music Choice.[53] He further cites a court ruling which found that "[M]any factors come into play in reaching and obtaining settlement (*sic*) and, as such, settlement payments could not be a reliable guide for computing the value of a reasonable royalty."[54] Based on this history and this ruling, he concludes "rates contained in settlement agreements are not necessarily indicative of a market rate" and that "there are many reasons why a settlement lacks reliability as to the true value of a royalty rate."[55]

(64) Dr. Wazzan appears not to realize, as summarized in Section II.C.1 above, that his sole benchmark, the CABSAT rate, has itself *only* been set as the basis of settlements between SoundExchange and the relevant parties paying that rate. *Based on his own arguments*, the CABSAT rate should therefore not be used as a benchmark for PSS rates in this proceeding.

II.D.2. The CABSAT settlements *themselves* prohibit their use as benchmarks

(65) Dr. Wazzan is not alone in his inconsistency. In the most recent CABSAT settlement agreed between SoundExchange and Sirius XM dated December 11, 2014, both parties agreed that such settlements

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[50] "Based on my review of previous proceedings, it appears that setting PSS rates has historically been challenging because of the relative lack of services sufficiently comparable to the PSS. That remains an issue today." (Wazzan WDT, ¶12) And "[R]elatively few example digital music services have had the key characteristics of the PSS... This difficulty appears to still exist." (Wazzan WDT, ¶22).

[51] "[I]t is not apparent how one might adjust the benchmarks Dr. Ford proposed to address the concerns of the Judges, such as the lack of comparability between these other types of services and the PSS and thereby derive a specific rate from the benchmarks." (Wazzan WDT, ¶50)

[52] Wazzan WDT, ¶¶24d, 64.

[53] Wazzan WDT, ¶¶35, 36.

[54] Wazzan WDT, ¶41.

[55] *Ibid.*

would be *non-precedential*.[56] In particular, both parties agreed that the "royalty rates and terms [agreed in the settlement] shall not be relied upon as precedent in any proceeding to set statutory royalty rates and terms (other than the [CABSAT] Proceeding)." That SoundExchange is proposing them as a benchmark in this proceeding clearly violates this provision.[57]

(66) Furthermore, negotiation documents provided to counsel for Music Choice in the discovery process show that [[ ]].[58] In particular, they show that [[ ]]

(67) This history of the current CABSAT negotiations shows two things. First, [[ ]]. Thus SoundExchange has itself agreed not to use the CABSAT market as a potential benchmark for the PSS (or any other) market [[ ]] (until ignoring that provision in this proceeding).

(68) Second, it shows that SoundExchange [[ ]] That SoundExchange would allow its expert to use the CABSAT rates as a benchmark after expressly agreeing that they could not be used this way is disquieting. Based on SoundExchange's own agreements, the CABSAT rate should therefore not be used as a benchmark for PSS rates in this proceeding.

II.D.3. CABSAT rates are *not* workably competitive marketplace rates and Dr. Wazzan provides no adjustments to account for this fact

(69) Putting aside both Dr. Wazzan's and SoundExchange's inconsistencies, there are two important economic reasons for dismissing the CABSAT rate as a benchmark for the hypothetical PSS market.

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[56] Item 4 in the settlement, titled "Agreement Non-Precedential," states "The royalty rates and terms set forth in the Proposed Regulations are intended to be nonprecedential in nature and based on the Parties' current understanding of market and legal conditions; among other things. Such royalty rates and terms shall be subject to *de novo* review and consideration in future proceedings." *See* Appendix D.1 CABSAT Settlement Agreement, SoundX_000477825.

[57] *See* Appendix D:1 CABSAT Settlement Agreement.

[58] *See* Appendix D.2 CABSAT Negotiation documents.

(70) First, as I describe in my own direct report, an ideal benchmark market involve *marketplace outcomes*.[59] On this, Dr. Wazzan and I agree: his report is replete with preferences for marketplace benchmarks. Unfortunately, he concludes "I have … identified no *marketplace* benchmark that is sufficiently comparable to the PSS to be used for this purpose…."[60] As discussed above, he ultimately relies on (unadjusted) CABSAT rates as a benchmark for PSS.[61]

(71) This is an unsupportable conclusion. CABSAT rates are not representative of rates that would arise in a hypothetical market for PSS sound recording performance rights for at least four reasons. First, as discussed in Section II.C.1 above, CABSAT rates have always been determined as the result of negotiations between a single seller, SoundExchange, and a small number of buyers. For example, the most recent CABSAT settlement on which SoundExchange is basing its rate request was the result of a settlement between it and only a single buyer, Sirius XM.

(72) Outcomes between a single buyer and a single seller can hardly be considered representative of a *workably competitive* market. Indeed, as I discuss in my direct report, the hypothetical market for PSS sound recording performance rights would be one between multiple *competing* record labels and one or more PSS providers.[62]

(73) The Judges in their Web IV decision discussed at length exactly this point, albeit in the context of rates for the non-interactive webcasting market. They recognized both the problem of *complementary oligopoly*, the idea that "firms offering complementary products," like the major record companies, "tend to set higher prices than would even a monopoly seller of the same products, illustrating that suppliers of complements do not compete with one another," as well as the role that competitive "steering" (the willingness of some record companies to accept a reduced per-play royalty in the non-interactive webcasting market in return for a higher share of plays) plays to mitigate such an effect.[63] Indeed, "The Judges [found] that steering in the hypothetical noninteractive market would serve to mitigate the effect of complementary oligopoly on the prices paid by the noninteractive services and therefore move the market toward effective, or workable, competition. Steering is synonymous with price competition in this market, and the nature of price competition is to cause prices to be lower than in the absence of competition, through the ever-present 'threat' that competing sellers will undercut each other in order to sell more goods or services."[64] In a nutshell, "the Judges find the

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59 Crawford WDT, ¶50.

60 Wazzan WDT, ¶12 (emphasis in original).

61 Wazzan WDT, ¶12.

62 Crawford WDT, ¶¶43-44.

63 Library of Congress, 37 CFR Part 380. *Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings (Web IV). Final Rule*, 81 Fed. Reg. 26,316, 26,342 (May 2, 2016). Hereinafter, "Web IV."

64 Web IV, FR 26,366.

economic opinion expressed by Dr. [Carl] Shapiro (the economic expert for Pandora in Web IV) — equating steering with price competition—to be correct."[65]

(74) While the fact that SoundExchange negotiated the CABSAT agreement might help resolve some concerns about complementary oligopoly, it certainly does not equate such an outcome with a *workably competitive* market. Instead, a workably competitive market would involve sellers actively competing for each other's business (i.e. more plays on a buyer's service) by means of a lower royalty rate. As noted by Dr. Shapiro, the effect of a *willingness* of suppliers to compete with each other would lower prices in the hypothetical non-interactive market, even if the "net result in a workably competitive market may well be relatively little *actual* steering." (emphasis added).[66]

(75) The exact same forces would be at play in a workably competitive hypothetical market for PSS sound recording performance rights. Rates would be lower than that provided either by complementary oligopolists *or* by the monopolist SoundExchange. Dr. Wazzan neither acknowledges nor adjusts for this important difference between the CABSAT market and the hypothetical PSS market.

(76) Second, outcomes in a workably competitive market should not be influenced by considerations in other markets, or, if so influenced, they should be adjusted for this fact. As discussed in Sections II.C.1 and II.C.3 above, the CABSAT market amounts to less than [[ ]] of Sirius XM's company-wide revenue and Sirius XM and SoundExchange both acknowledge that Sirius XM treats its CABSAT service as a promotional vehicle for its SDARS service.[67] In such a case, the decisions Sirius XM makes when negotiating CABSAT rates *cannot* be considered comparable to a buyer like Music Choice in a hypothetical PSS market for whom the PSS market is its only consideration (and for whom the royalty it pays for sound recording performance rights is an essential determinant of its long-run viability).

(77) Third, the rates negotiated between SoundExchange and Sirius XM that form the basis of SoundExchange's rate submission (and supported by Dr. Wazzan) are not *marketplace* rates unfettered by regulatory "overhang." Indeed, the actual settlement agreement makes this exact point: both SoundExchange and Sirius XM agreed that the rates could not be used as benchmarks in any other rate proceedings because they reflected not only market conditions, but also "legal conditions" and "other things."[68]

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[65] Web IV, FR 26,367.

[66] Web IV, FR 26,357 citing Shapiro WDT at 9.

[67] As discussed in Section II.C.2.a Muzak's and DMX's contracts with DISH Network and DirecTV are similarly influenced by considerations in other markets, in their case by the desire to obtain satellite distribution for their commercial background music service.

[68] *See* Appendix D.1 CABSAT Settlement Agreement, SoundX_000477825 (Item 4 in the settlement, titled "Agreement Non-Precedential," states "The royalty rates and terms set forth in the Proposed Regulations are intended to be nonprecedential in nature and based on the Parties' current understanding of market and legal conditions; among other things. Such royalty rates and terms shall be subject to *de novo* review and consideration in future proceedings.")

(78) Furthermore, the CABSAT rates negotiated by Sirius XM necessarily reflect the costs and benefits to them of the alternative to a settlement, which is a CABSAT rate determination by the Copyright Royalty Judges. As further discussed in Section II.C.3 above, the expected costs to Sirius XM of pursuing a CABSAT rate determination would very likely exceed the expected benefits. In such an environment, SoundExchange has tremendous bargaining power in settlement negotiations and could reasonably expect to extract almost all of the surplus Sirius XM earns from its CABSAT service. The fact that Sirius XM pays royalty rates for its CABSAT service in excess of [[ ]] strongly suggests that both parties realized this and that SoundExchange was able to impose just such an outcome. In such a case, Sirius XM *again* cannot be considered comparable to a buyer in a hypothetical PSS market like Music Choice for whom such negotiations are the lifeblood of their business.

(79) Fourth, in justifying his use of CABSAT rates as a benchmark, Dr. Wazzan argues that "the applicable rate standard is the willing buyer/willing seller standard under 17 U.S.C. § 114(f)(2)."[69] From this, he concludes, "Thus, they purport to be fair market rates."

(80) This is simply a wrong conclusion. While that may be the CABSAT rate *standard*, the Copyright Royalty Judges (or their predecessors) have *never* issued a CABSAT rate ruling under this standard. Instead, as summarized in Section II.C.1 above, in each of the three relevant CABSAT proceedings, they have adopted the rates reached in settlement negotiations between the relevant parties. In the case of such settlements, the Judges may not independently review and amend the rates unless there is an objection from a participant in the proceeding, meaning that *there is no reason to believe that such settled rates reflect the outcome of a competitive market for sound recording performance rights.*[70] Dr. Wazzan certainly advanced no evidence that the CABSAT rates actually reflect marketplace rates and my analysis of the CABSAT market in this section concludes that these are not outcomes representative of a workably competitive hypothetical market for PSS sound recording performance rights.

(81) As Dr. Wazzan fails to acknowledge these differences between CABSAT and true marketplace outcomes, he makes none of the adjustments necessary to account for them. He does not adjust his recommended CABSAT rate for the effects of any differences in negotiations between SoundExchange and Sirius XM versus those that would arise between competing record labels and one or more PSS providers. He does not adjust his recommended CABSAT rate for the fact that Sirius XM treats it as a promotional service and not as a core business as would a PSS provider. And he does not adjust his recommended CABSAT rate for the effects of any differences in the costs and

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[69] Wazzan WDT, ¶64.

[70] Section 801(b)(7)(A) of the Copyright Act authorizes the Judges to either adopt rates and terms negotiated by the settling parties or to decline to adopt the agreement, with the latter decision possible only if a participant objects and the Judges conclude that the agreement does not provide a reasonable basis for setting statutory terms or rates. There are no provisions in this section of the Copyright Act that would allow the Judges to amend or reject the negotiated rates and terms if all participants have agreed to those terms. (Section 801. Copyright Royalty Judges; appointment and functions. https://www.copyright.gov/title17/92chap8 html.)

benefits of a rate proceeding between Sirius XM in the CABSAT market and how outcomes would arise in a hypothetical PSS market. For all these reasons, the Judges should therefore reject the CABSAT rates as a benchmark informative of PSS marketplace outcomes.

II.D.4. CABSAT rates are the result of different cost and demand conditions and Dr. Wazzan provides no adjustments for these differences

(82) When teaching students how to think about the processes generating outcomes in product markets, I often encourage them to think of these processes as the interaction of demand, cost, competition, and – in some markets – regulation. In the previous subsection, I described how Dr. Wazzan fails to account for the difference between CABSAT outcomes and marketplace outcomes that would arise in the hypothetical market for PSS sound recording performance rights. That discussion focused on the last two of these factors: how unadjusted differences in competitive conditions and the impact of regulation between the CABSAT and hypothetical PSS markets make CABSAT rates unusable as a benchmark in this proceeding. In this section, I provide a second set of economic reasons for reaching the same conclusion due to differences in the cost and demand structures in the two markets.

(83) I consider first differences in the costs of serving the (hypothetical) PSS and (actual) CABSAT markets. While there are two remaining PSS services, the largest by far (and only one actively competing for business) is Music Choice.[71] As discussed in my direct testimony, Music Choice has three lines of business: a residential audio service consisting of its audio music channels, a residential video service consisting of a music video channel called MC Play and a video-on-demand (VOD) service called Music Choice On Demand, and a commercial audio service.[72] As described there, Music Choice bundles its residential audio and video services when negotiating licenses with cable systems. In 2016, 2017, and 2018, Music Choice estimates that its residential audio revenue will constitute [[ ]] of its total revenue.[73] As in my direct report, I use these values as indicative of Music Choice's likely future share of revenues accruing to its audio business. I conclude from this that Music Choice's primary line of business for the period 2018-2022 will be the PSS market. As discussed in my direct report, the majority of Music Choice's costs are also dedicated to serving this market.

(84) When considering the costs of serving the CABSAT market, I focus on Sirius XM, as it was the only firm paying CABSAT rates that participated in the last settlement with SoundExchange that forms the basis of SoundExchange's rate proposal in this proceeding. I do this despite the facts discussed at

[71] Del Beccaro WDT, 44.

[72] Crawford WDT, 27-38.

[73] This decline is due to projections of [[ ]] Music Choice P&L, 2016-2022. [Privileged and Confidential - Consolidated BW 101316].

length above making Sirius XM non-comparable with a buyer like Music Choice in the hypothetical PSS market.

(85) Unfortunately, I do not know what will be Sirius XM's share of revenue from the CABSAT market for the years 2018-2022. Using the information from 2013-2015 presented in Table 2 as a rough guide, however, shows that in that period, Sirius XM's CABSAT business represented between only [redacted] of their total revenues. It is clear that the CABSAT market is not Sirius XM's primary line of business.[74]

(86) This difference has an important effect on the cost structure of a PSS provider like Music Choice and a CABSAT provider like Sirius XM. As I discuss in detail in Section II.E below, firms for which the CABSAT market is not a primary line of business need not recover all of their fixed costs of operations from that market.[75]

(87) Firms that are subsidizing the CABSAT market using other lines of business will typically have lower costs of serving the CABSAT market than would Music Choice of serving the PSS market. While present, however, the size of this cost difference is uncertain. As Sirius XM appears to simply rebroadcast some of its satellite music channels over DISH Network, its incremental costs may be quite small.[76] What is definitely true is that Dr. Wazzan has not provided any evidence about the costs Sirius XM must incur to offer its CABSAT service, nor has he compared those costs to either those likely to be incurred by a PSS provider in the hypothetical PSS market or those actually incurred by Music Choice and made available in this proceeding.

(88) I consider next differences in the demand for products offered in the PSS and CABSAT markets. As for costs, I focus on Music Choice in the PSS market and Sirius XM in the CABSAT market. There are immediately some important differences, differences that would necessarily need to be accounted for if one were to use rates in the CABSAT market as a benchmark for rates in the PSS market.

(89) The leading PSS provider, Music Choice, offers both music audio channels as well as a music video channel and a very popular VOD service. As described in the testimony of both Music Choice CEO

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74 Furthermore, Sirius XM has been profitable, with reported net income between $376.8 million in 2013 and $509.7 million in 2015, and likely will continue to be profitable in the 2018-2022 period (Sirius XM 2015 10-K, F-4). In announcing the 2016 results CEO Jim Meyer commented "Last year was a phenomenal year for Sirius XM's business, and we expect continued success in 2017. We finished ahead of our guidance across the board, with record revenue, adjusted EBITDA and free cash flow. With more than 31 million subscribers, Sirius XM has never had more paying customers. We've issued guidance for continued growth in 2017, and we expect a record adjusted EBITDA of more than $2 billion." *See* Sirius XM Press Release, "Sirius XM Reports Fourth Quarter and Full-Year 2016 Results," Feb. 2, 2017, http://investor.siriusxm.com/investor-overview/press-releases/press-release-details/2017/SiriusXM-Reports-Fourth-Quarter-and-Full-Year-2016-Results/default.aspx.

75 Fixed costs include all non-royalty operating and capital costs.

76 Sirius XM states the following regarding its "Satellite Television Service" which is part of its other services category: "Certain of our music channels are offered as part of certain programming packages on the DISH Network satellite television service." (Sirius XM 2016 10-K, 5.)

David Del Beccaro and Senior Vice President of Programming Strategy and Partnerships Damon Williams, Music Choice also invests significant resources in the quality of its music programming. Furthermore, [[ ]].[77] All of these services are bundled together in contracts with cable systems.

(90) By contrast, Sirius XM does not offer a video music channel nor a VOD service. This lowers the value of its service to households and thus to the cable operators that would contract with them. To this point, Music Choice estimated that between 2012 and 2014 they were able to win contracts in competition with Stingray, the only CABSAT provider active in the cable radio market, despite receiving an estimated [[ ]] price premium due to Stingray's lack of a competitive VOD offering.[78] As Sirius XM does not actively compete for business with Music Choice, the price premium Music Choice could command relative to Sirius XM is simply unknown.

(91) Furthermore, there are other important quality differences between the two services. First, I understand that Sirius XM does not allow Internet or mobile app access as part of its CABSAT offerings and that, because they treat it as promotional, they don't provide their full suite of audio channels on their CABSAT service.[79] Second, Music Choice has documented the significant resources it expends on programming staff. While Sirius XM no doubt also has significant programming staff, Dr. Wazzan has not provided any evidence about the nature of Sirius XM's cable radio programming and programming expenses. Finally, while both Sirius XM and Music Choice offer a suite of audio music channels, the majority of Sirius XM's listeners listen in their cars, while Music Choice's listeners watch/listen on a television in their home. This could well have important differences for the types of music played as well as the types of efforts each firm exerts providing useful on-screen information. While very useful in an at-home environment, too much on-screen information in the car might actually be unsafe!

(92) Taken together, the analysis in this subsection demonstrates that there are many important differences in the cost and demand characteristics of Sirius XM's CABSAT service and the cost and demand characteristics of Music Choice's PSS service. As Dr. Wazzan has not acknowledged any of these differences, he has not provided any testimony to help evaluate them or to make the necessary adjustments to the CABSAT rate to account for them (were the Judges to consider it a useful benchmark).

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77 Crawford WDT, ¶24.

78 Crawford WDT, ¶147. Stingray also does not appear to offer a linear music video channel like MC Play and, as discussed in Section III.C below, there appear to be important quality differences between the Stingray Music and Music Choice audio channels. These could also be factors in the price premium perceived by Music Choice.

79 Del Beccaro WRT, 3-4.

(93) Instead, Dr. Wazzan's "analysis" of the potential differences between the PSS and CABSAT markets amounts to a handful of paragraphs. He concludes (without justification) that "[t]he PSS and the CABSAT services have the same functional characteristics," ignoring the differences in the quality of PSS versus CABSAT services described above.[80] He further concludes that "PSS and the CABSAT services compete for the same MVPD wholesale buyers,"[81] ignoring that the only party to the CABSAT settlement, Sirius XM, in fact does not compete for the same MVPD wholesale buyers and that Stingray, who does compete for such buyers, was not a party to the settlement and, for the reasons described in Section II.C.4 above, has yet to show they can compete effectively in this market in the long run paying CABSAT rates.

(94) Furthermore, just as he makes *no adjustments* for the fact that the differences between CABSAT and hypothetical marketplace rates, he similarly makes *no adjustments* for the differences in cost and demand characteristics between the CABSAT and hypothetical PSS market. I therefore conclude again that the Judges should reject CABSAT rates as a benchmark informative of PSS marketplace outcomes.

II.E. If adopted, Wazzan's arguments imply that no PSS provider could offer a PSS service as a standalone business, limiting competition and harming consumers

(95) The analysis above showed that, whether by Dr. Wazzan's own arguments, SoundExchange's existing agreements, or by an analysis of the differences between the CABSAT and PSS markets for sound recording performance rights, CABSAT rates cannot serve as an effective benchmark for the hypothetical PSS market. This subsection develops one of the points raised above in greater detail, namely that each and every firm paying CABSAT rates offers a service that is *ancillary* to its primary line(s) of business. I show below that, if the judges were to institute a PSS sound recording performance royalty based on CABSAT rates, that *no PSS provider could offer a PSS service as a standalone business.* This is contrary to the purpose of this proceeding, would limit competition, reduce quality, and harm consumers, and would not be achievable in a workably competitive hypothetical market.

II.E.1. An economic framework for evaluating the implications of Dr. Wazzan's proposal

(96) To explain this implication of Sound Exchange's and Dr. Wazzan's proposed rates requires an understanding the economics of providing products in a market environment. In any market, there are

[80] Wazzan WDT, ¶62f.

[81] Wazzan WDT, ¶62g.

two kinds of costs that require the attention of any firm providing a service in that market. The first are *fixed costs*, costs that must be paid regardless of how many customers ultimately buy and consume the product. Examples of fixed costs include the cost of buildings, equipment, capital, and staff that are necessary to provide a service regardless of the number of customers. The second are *marginal costs*, costs that vary with the number of customers that buy and consume a product. Examples of marginal costs are royalties that increase with the number of subscribers, and thus the revenue of the firm. Marginal costs are often also called variable costs.

(97) In order for a firm to be profitable, it must cover both its fixed and marginal costs, including its cost of capital (i.e. the cost necessary to raise money to invest in the firm). In microeconomics, much of the analysis of *pricing* depends on marginal costs: a firm's optimal price (if it has pricing power) is often written as a function of its marginal costs plus a markup term which depends on how differentiated its product is relative to other products in the market. But the analysis of *product offerings* typically depends on fixed costs: *given* a firm's optimal price, the firm can calculate its *variable profits* (or contribution margin), i.e. the profits it receives from the sales of its goods before accounting for fixed costs. In order to offer a product, or to serve a market, it must be the case that a firm's variable profits exceed its fixed costs. If not, then even if it makes positive profit on each unit it sells, the sum of this profit across all units isn't sufficient to cover its fixed costs of operation and it must necessarily not offer that product/serve that market (or go out of business if it is the firm's only product).

II.E.2. A PSS royalty based on a CABSAT rate is economically unsustainable and will not permit a standalone provider of US cable radio services

II.E.2.a. Overview

(98) Building on the simple theory presented above, if a firm has only a single product line, then for it to stay in business it must be the case that the variable profits from that product line exceed the fixed costs of offering that product line. If a firm has multiple product lines, however, then for it to stay in business it must be the case that the variable profits across all product lines exceed the fixed costs of offering all product lines.

(99) A corollary to this theory is that if a regulator sets a cost for a service at too high a level, then it may not be possible for a single-product firm to cover this cost while it is possible for a multi-product firm to do so. If this arises, the regulator is essentially mandating that the market be served by multi-product firms that can subsidize the market in question with profits from their other lines of business.

(100) This is relevant in the market for PSS sound recording performance rights because if firms face fixed costs for serving their primary line of business, but fewer fixed costs than would a standalone firm for

providing a CABSAT service, then they might be able to offer a CABSAT service at lower cost than would a standalone firm, *even if this service is less attractive to consumers*.

(101) In this subsection, I demonstrate that setting a PSS rate at the CABSAT level, as supported by Dr. Wazzan's testimony, would not permit a standalone provider of US cable radio services. I motivate this line of reasoning in three steps. First, I calculate the "net revenue" (i.e., CABSAT revenue minus CABSAT royalties) for each of the CABSAT providers in the 2013-2015 period, the years for which I was able to obtain revenue and royalty data, and use these as a rough estimate of the maximal variable profits of their CABSAT services in the 2018-2022 period at issue in this proceeding. Second, I calculate the fixed costs of serving the PSS market on a stand-alone basis. For this, I use financial data from Music Choice, the only large-scale PSS provider. Third, I compare the net revenues to these fixed costs and demonstrate that none of the CABSAT providers would be able to profitably serve the CABSAT market paying the costs of a stand-alone PSS provider. I then also show that Music Choice itself would not be able to profitably serve the PSS market if it had to pay CABSAT royalty rates. Thus, setting a PSS rate based on the CABSAT royalty would *necessarily* prevent *any* stand-alone provider of PSS services. In the next subsection, I discuss the implications of such a decision by the Copyright Royalty Judges.

II.E.2.b. The profitability (or lack thereof) of a stand-alone PSS service for CABSAT providers at CABSAT rates

(102) I begin evaluating the profitability of a stand-alone PSS service for CABSAT providers paying CABSAT rates by referring to Table 4 above. It showed, for each firm offering CABSAT services, the "net revenue" of that service, i.e. the total revenue each firm received from its CABSAT service after paying CABSAT sound recording performance royalties to SoundExchange. Table 5 below repeats this information, adding two additional pieces of data.

(103) This net revenue is an *upper bound* on the variable profit each firm could possibly have received from its CABSAT service: such royalties are clearly a marginal cost and so the revenue left after paying them will be part of variable profit, but there are undoubtedly other marginal costs (such as musical works royalties) not included in this calculation that would yield a lower variable profit. Using such an upper bound on variable profit renders the remainder of my analysis in this section conservative.

(104) The second through fourth columns of Table 5 below report the net revenue for each CABSAT service provider. For DMX, because it pays more than [[ ]] of its CABSAT revenues as royalties, even this upper bound on variable profits [[ ]]. It is therefore no surprise that Mood Music began serving DMX customers with its Muzak audio channels; by doing so it could reduce its sound recording performance royalties to the PSS rate and, perhaps, make some variable profits by doing so.

(105) Even so, none of the CABSAT providers earns much in the way of net revenue from its CABSAT service. The greatest is for [[ ]] in 2015, when it received in net revenue from the CABSAT market.

Table 5: Net revenue and maximum economic profit for CABSAT firms providing a CABSAT service on a stand-alone basis

In thousands	Sirius XM net revenue	DMX net revenue	Stingray net revenue	Fixed cost (non-royalty operating expenses and capital expenses)	Stingray economic profit

Sources: Sirius XM: SoundX_000145768, SoundX_000145778, SoundX_000145782; Stingray: SoundX_000145790, SoundX_000145813, SoundX_000145808; and DMX: SoundX_000145804, SoundX_000145801. Net revenue is calculated as (CABSAT revenue – CABSAT royalty costs). Fixed cost include non-royalty expenses and capital expenses. *See* Table 6 and Exhibit B.1. Economic profit (loss) is calculated as net revenue – fixed cost.]]

(106) In order to be profitable, however, firms also need to recover their fixed costs. I next calculate the fixed costs of providing a stand-alone cable audio service. As Music Choice is the largest and longest-standing PSS provider, I use their fixed costs as an estimate of the fixed costs necessary to serve the PSS market on a stand-alone basis. I further assume that Music Choice's fixed costs are a good estimate of the fixed costs necessary to provide a CABSAT service on a stand-alone basis.

(107) To estimate these fixed costs, I rely on the same detailed financial information from Music Choice as I did in my written direct testimony. As I did there, I use Music Choice's financial information from the period 2016-2018 as my best estimate of their future performance in the 2018-2022 period at issue in this proceeding.[82]

(108) As I did in my written testimony, to estimate Music Choice's fixed costs I only considered those costs that could be allocated to Music Choice's residential audio business.[83] These costs can be broken down into three parts: royalty expenses, non-royalty operating expenses, and capital expenses. Music Choice's royalty expenses (for both sound recording and musical works performance rights) are clearly marginal costs: they increase and/or decrease as Music Choice attracts more MVPD customers and/or negotiates higher or lower rates with these customers and then pays royalties on those revenues.

(109) The vast majority of Music Choice's non-royalty operating expenses and capital expenses are, by contrast, fixed costs. Music Choice's non-royalty operating expenses include the costs of

[82] Crawford WDT, ¶115-120.

[83] *See* Crawford WDT, ¶124-134.

programming and operations, sales and marketing, G&A (general and administrative), D&A (depreciation and amortization), and other expenses.[84] Music Choice's capital expenses are Music Choice's residential audio business' invested capital times their cost of capital.[85] They are necessary to produce all of the music channels offered on the service and would be necessary whether Music Choice served 1 customer or the 40 million that they currently serve.[86]

(110) Exhibit B.1 in the Appendix reports these marginal and fixed costs for Music Choice for 2016-2018.[87] Based on Music Choice's predicted future financial performance, I estimate that they would face fixed costs of [redacted] for its residential audio business. The lowest of these fixed costs is [redacted] I include this as the fourth column in Table 5. In the fifth column of Table 5, I calculate the economic profit or loss (net revenues minus fixed costs) that would accrue to [redacted] the most profitable of the CABSAT service providers, if it had to pay the fixed costs of a stand-alone PSS service.[88]

(111) A quick glance at Table 5 demonstrates that even the greatest net revenue of *any* of the firms that currently offers CABSAT services would be wholly insufficient to cover the fixed costs of providing such a service on a standalone basis. The most profitable scenario is for [[[redacted]]] in 2015, when its revenues of [redacted] would be reduced by fixed costs of [redacted].[89] *No* CABSAT provider could profitably serve the CABSAT market on a standalone basis; each *needs* to offer another profitable service to help defray the fixed costs of offering a CABSAT service.

II.E.2.c. The profitability of Music Choice as a standalone PSS at proposed CABSAT rates

(112) My analysis to this point has focused on the three firms *currently* paying CABSAT rates. What if Music Choice were required to pay CABSAT rates for the 2016-2018 period I am using to form my fixed cost estimates? Would Music Choice be profitable on a standalone basis?

(113) Table 6 *demonstrates that it would not*.[90] The second column of Table 6 calculates the share of Music Choice's estimated unadjusted residential audio service revenue that would accrue to sound recording

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[84] *See* Exhibit B.1: Music Choice Residential marginal costs, non-royalty operating expenses, and capital expenses.

[85] It is calculated by multiplying the capital expense ratio of [redacted] (itself given by Music Choice's average capital expenses divided by its unadjusted residential audio revenue during 2013-2015 as shown in Crawford WDT Exhibit B.2) and Music Choice's unadjusted residential audio revenues during 2016-2018. (Crawford WDT Exhibit B.3.)

[86] From Music Choice, I learned that a very small portion [redacted] of these non-royalty operating costs vary with usage, and thus the number of subscribers. For simplicity and to match the cost line-items presented in my written direct report, I chose not to move these to the marginal cost category. Needless to say, doing so would have had no material impact on my analysis.

[87] *See* Exhibit B.1: Music Choice Residential marginal costs, non-royalty operating expenses, and capital expenses.

[88] *See* Crawford WDT, ¶151-154.

[89] My estimate of Stingray's net revenues are lower-bound because I do not subtract the musical works royalties (as I do not have this information available to me).

[90] The last column in Table 6 shows that Music Choice's economic losses range from [redacted]

performance royalties in each of 2016, 2017, and 2018 if they were to pay the CABSAT rate in those years.[91] It shows that it would pay between [redacted] in sound recording performance royalties, far greater than the 8.5% PSS rate.[92]

Table 6: Music Choice's financial performance under CABSAT rates

Amounts in thousands	CABSAT revenues paid as royalties	Net revenue	Fixed costs (non-royalty operating expenses and capital expenses)	Economic profit (loss)
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Sources: Music Choice P&L forecast (revenue and cost) data, Music Choice digital subscriber forecast data, SoundExchange proposal for royalty per-subscriber ($0.0179 in 2016, $0.0185 in 2017, and $0.0190 in 2018) and capital cost ratio as calculated in Exhibit B.2 in Crawford WDT. Note: Music Choice's CABSAT royalty is calculated at the CABSAT rates for its digital subscribers (average of beginning and end-of-year figures) and the CABSAT revenues are based on the unadjusted revenues for the royalty share. Net revenue is calculated as (10% VOD-adjusted residential audio service revenue – audio royalty costs). Audio royalty costs include CABSAT royalties and PRO royalties. Fixed costs include non-royalty operating costs and capital costs. Economic profit (loss) is net revenues minus fixed costs (non-royalty operating costs and capital costs. *See also* Exhibit B.1 and Exhibit B.2.]]

(114) The third column of Table 6 shows the net revenues implied by these calculations. It takes Music Choice's [[redacted]] VOD-adjusted residential audio service revenue and subtracts both the CABSAT-level sound recording performance royalty and its existing musical works performance royalty.[93]

(115) Appendix Exhibit B.2 shows the calculation underlying these values. These net revenues vary from [redacted] The remaining columns in Table 6 compare Music Choice's net revenues to their estimated fixed costs in each year from 2016-2018. These fixed costs (non-royalty expenses and capital expenses) are the same as those described earlier and reported in Exhibit B.2 in the Appendix. In each year, Music Choice's net revenues after paying CABSAT royalties are less than their fixed costs in that year, yielding losses on their residential audio service business of between [redacted]]] Paying CABSAT-level royalties for sound recording performance rights, Music Choice would necessarily lose significant sums of money and exit the PSS market.

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[91] The VOD-adjusted residential audio service revenue is the sum of Music Choice's residential advertising revenue and its reported residential audio license fees adjusted by [[redacted] to account for the value of video-on-demand service that is bundled and does not have a separate fee. This adjustment is a conservative adjustment in comparison to Music Choice's estimated premium for the VOD service of [redacted] based on the ability to win contracts by this premium when faced with competition from a competitor without VOD service. *See* Written Direct Testimony of Gregory S. Crawford, PhD, ¶¶146-149.

[92] The average CABSAT royalties as a percentage of the unadjusted revenues is [redacted] during 2018–2022.

[93] I subtract the musical works royalty as that too is clearly a marginal cost that would be taken out when calculating variable profits. I do not subtract a musical works royalty for the three firms paying CABSAT sound recording performance royalties in Table 4 and Table 5 as I do not know the royalty rate they pay for musical works and failing to do so simply increases my estimate of their (maximum) variable profits, making my analysis conservative.

(116) If Music Choice, the firm that makes the greatest variable profits in the PSS market, cannot cover the fixed costs necessary to serve the PSS market on a standalone basis paying CABSAT royalties, then no one can. In other words, *no firm could pay sound recording royalties at CABSAT levels and profitably serve the cable radio market on a standalone basis.*

II.E.3. Requiring a PSS provider to necessarily offer another service is contrary to the mandate in this proceeding, reduces competition, harms consumers, and imposes an outcome that would not be implementable in the absence of this rate proceeding

(117) Imposing a royalty that doesn't allow a standalone PSS provider is objectionable on both procedural and economic grounds. Procedurally, I understand that the mandate of the Copyright Royalty Judges is to set rates for PSS providers taking into account *only* the economic environment in the PSS market.[94] It should not account for other products and services offered by the same firms (e.g. Music Choice's residential video business) nor require firms to offer other products and services in order to serve the PSS market.

(118) Economically, imposing a royalty that doesn't allow a standalone PSS provider increases the barriers to entry of serving the US cable radio market by requiring a significant portion of the fixed costs of providing US cable radio services to be covered by another line of business. For Sirius XM, this is the satellite radio market. For DMX, this is the commercial background music market. For Stingray, this is the Canadian cable radio market, and its other business lines such as Music Choice International, Concert TV, and The KARAOKE Channel. The most relevant of these is of course Stingray Music, as it is the *only* CABSAT provider competing for business in the United States. Surely the Judges would not agree that the only way a company could provide a PSS service in the United States is if they are a foreign company with no fixed infrastructure in the United States?

(119) If the Judges approve a PSS rate at the level proposed by SoundExchange, standalone PSS providers like Music Choice would simply be forced out of the market. This would have at least three important follow-on consequences.

[94] For example, in the first PSS proceeding, all of the services (DMX, Muzak, and Music Choice, then called Digital Cable Radio), offered commercial services. *In Re: Determination of Statutory License Terms and Rates for Certain Digital Subscription Transmissions of Sound Recording*, No. 96-5 CARP DSTRA, Report of the Copyright Arbitration Royalty Panel, (Nov. 12, 1997), ¶47. Despite this, the Copyright Arbitration Royalty Panel (CARP) appears only to have considered each service's PSS business in making its determination. For example, when discussing the third 801(b) factor, it concluded "In making its determination, the Panel balanced the costs and risks involved in producing the sound recordings against the cost and risks associated with bringing the creative product to market in a new and novel way." Library of Congress, Copyright Office, 37 CFR Part 260, [Docket No. 96-5 CARP DSTRA], *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings. Final Rule and Order*, 63 FR 25,394, 25,407 (May 8, 1998). Hereinafter CARP 1998.

(120) First, the forced exit from the market of standalone PSS providers like Music Choice would *reduce competition in the PSS market.* Reduced competition generally leads to higher consumer prices and less innovation, causing direct harm to consumers.

(121) Second, the forced exit from the market of Music Choice in particular would *lower the quality* of PSS services. Requiring that the products that serve the PSS market are those that necessarily have been developed for other lines of business (e.g. Canadian cable radio) means that consumers in the PSS market will either not have access to some popular PSS products (video channels) or will have access to lower-quality versions of those products.[95] This unequivocally harms consumers.

(122) Finally, *imposing a CABSAT rate in the PSS market implements a market outcome that would not be possible in the absence of this rate proceeding.* As established in the previous subsection, a royalty set at the CABSAT level would cause Music Choice, the largest and most successful PSS provider, to incur losses between [redacted] per year. Under this financial burden, they would be forced from the market.

(123) With the exit of Music Choice, cable operators would scramble to provide music channels to their subscribers. While each of the extant CABSAT providers likely faces lower costs for serving these subscribers than Music Choice, so too are their services likely to be less attractive to cable operators. And their CABSAT royalty costs would clearly be much higher. It is therefore impossible to know with the information I currently have available whether any would be viable serving the PSS market at CABSAT rates, but, as described in Section II.C.4, the history of the CABSAT market is not encouraging in this regard. Of course, each CABSAT provider could subsidize their CABSAT services using the profits from their primary lines of business, but it would not be in their interest to do so if it *lowered* their overall profitability. In my opinion, the most likely outcome would be that SoundExchange would lower the rates it charges CABSAT providers to a level that would allow them to remain viable. *Neither SoundExchange nor Dr. Wazzan has presented any evidence to suggest whether such a rate would be higher or lower than the existing PSS rate.*

(124) Note that the converse of this proposition is *not* true: there is nothing that prevents existing firms paying CABSAT rates from competing for business with firms paying PSS rates; indeed this is exactly what is happening between Music Choice and Stingray. If indeed, Stingray has a better quality-cost proposition than Music Choice (without subsidizing their CABSAT operations with Canadian profits), then they will earn business from them in the long run *without the need for the Copyright Royalty Judges to jump-start the process.* Furthermore, if they perceive the CABSAT rates to be unfairly high and thus a competitive disadvantage relative to Music Choice's PSS rates, they

[95] As described in Section II.D.4 above, this view is supported by the fact that Music Choice currently offers some products some CABSAT providers don't (a music video channel and music VOD) and, even where a CABSAT provider does offer these channels, those from Music Choice are higher-quality offerings, for example a detailed on-screen information about the artist, song, and year of release.. *See also* Section III.C which documents some of the quality differences between Music Choice and Stingray Music.

need only participate in the next CABSAT proceeding and seek to convince the Judges that the existing CABSAT rates aren't those that would arise in a workably competitive hypothetical market for CABSAT services. Based on the analysis in this rebuttal report, I conclude that they would have a good case.

II.F. Wazzan's conclusions are even more inappropriate when accounting for the 801(b) policy factors

(125) In the previous two subsections, I have shown that the rates for PSS sound recording performance rights based on the CABSAT rates as proposed by SoundExchange and supported by Dr. Wazzan's testimony are (1) an inappropriate benchmark as they do not reflect the hypothetical PSS market and Dr. Wazzan does not adjust for the many differences between them and (2) that they would necessarily prevent a standalone provider of PSS services. All of the arguments made in support of these conclusions were based on economic principles and did not account for the 801(b) policy factors under which PSS rates are mandated to be chosen. In this subsection, I argue that relying on a CABSAT rate is even *more* inappropriate when accounting for the 801(b) factors as the 801(b) rate standard was put into place to protect PSS providers and a CABSAT rate would do just the opposite.

II.F.1. The 801(b) policy factors were put into place to *protect* PSS providers and, while there need be no connection between 801(b) and marketplace rates, if the latter are used, then the upper bound of 801(b) rates should be *no higher* than market rates.

(126) As described in the testimony of Music Choice CEO David Del Beccaro, when Music Choice entered the cable radio market, there was no sound recording performance royalty.[96] When Congress passed the Digital Performance Right in Sound Recordings Act of 1995 (DPRA), they therefore tried to carefully balance the interests of all affected parties.[97] First, they established a narrow digital performance right for sound recordings to prevent the introduction of interactive services from costlessly cannibalizing the record industry's recording sales.[98] Against this, they created a

[96] Del Beccaro WDT, 6.

[97] ("In particular, the Committee believes that recording artists and record companies cannot be effectively protected unless copyright law recognizes at least a limited performance right in sound recordings. Thus, S. 227 grants such a performance right, subject to various limitations intended to strike a balance among all of the interests affected thereby." . . . "In deciding to grant a new exclusive right to perform copyrighted sound recordings publicly by means of digital audio transmission, the Committee was mindful of the need to strike a balance among all of the interests affected thereby. That balance is reflected in various limitations on the new performance right that are set forth in the bill's amendments to section 114 of title 17. . . .") Senate Report. No. 104-128, Digital Performance Right in Sound Recordings Act of 1995, 14-16, https://www.congress.gov/104/crpt/srpt128/CRPT-104srpt128.pdf.

[98] ("[T]he Committee has sought to address the concerns of record producers and performers regarding the effects that new digital technology and distribution systems might have on their core business without upsetting the longstanding business and contractual relationships among record producers and performers, music composers and publishers and broadcasters that have served all of these industries well for decades. Accordingly, the Committee has chosen to create a

compulsory license to allow non-interactive services to license the music rights necessary to permit consumers to access music in new and innovative ways.[99]

(127) Establishing a compulsory license, however, also meant establishing a set of rules to govern the rates for such a license in the absence of agreements between rightsholders and rights users. While Congress could have chosen a market-based standard to set such rates, *they did not*: they chose to set rates for the new compulsory license using the 801(b) policy factors.

(128) Just three years later, the Digital Millennium Copyright Act of 1998 (DMCA) further amended the rules for digital performance rights. They established a willing buyer/willing seller standard for all new digital music performance services, but expressly required rates for pre-existing services (PSSs) to be set by the original, 801(b) policy standard.[100] Only Music Choice, Muzak, and the original DMX qualified as PSSs at that time.

(129) As described in 2006 by the Register of Copyrights, Congress relied on the 801(b) standard for PSSs because they "understood that the entities so designated as preexisting had invested a great deal of resources into developing their services under the terms established in 1995 as part of the [DPRA], and that those services deserved to develop their businesses accordingly."[101]

(130) This distinction in the rate standards for new digital music services on the one hand and PSS providers on the other clearly indicates that Congress intended to *protect* pre-existing providers who had entered the market and were offering services based on the expectation of not having to pay a sound recording performance royalty. A natural conclusion is that, *if* marketplace rates are used to

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carefully crafted and narrow performance right, applicable only to certain digital transmissions of sound recordings." … "This legislation is a narrowly crafted response to one of the concerns expressed by representatives of the music community, namely that certain types of subscription and interactive audio services might adversely affect sales of sound recordings and erode copyright owners' ability to control and be paid for use of their work.") Senate Report. No. 104-128, Digital Performance Right in Sound Recordings Act of 1995, 13, 15, https://www.congress.gov/104/crpt/srpt128/CRPT-104srpt128.pdf.

[99] ("This section amends section 115 of title 17 to clarify how the compulsory license for making and distributing phonorecords applies in the context of certain types of digital transmissions identified in the bill as 'digital phonorecord deliveries.'" . . . "The intention in extending the mechanical compulsory license to digital phonorecord deliveries is to maintain and reaffirm the mechanical rights of songwriters and music publishers as new technologies permit phonorecords to be delivered by wire or over the airwaves rather than by the traditional making and distribution of records, cassettes and CD's.") Senate Report. No. 104-128, Digital Performance Right in Sound Recordings Act of 1995, 36-37, https://www.congress.gov/104/crpt/srpt128/CRPT-104srpt128.pdf.

[100] Digital Millennium Copyright Act, 112 STAT. 2895 ("In establishing rates and terms for preexisting subscription services and preexisting satellite digital audio radio services, in addition to the objectives set forth in section 801(b)(1), the copyright arbitration royalty panel may consider the rates and terms for comparable types of subscription digital audio transmission services and comparable circumstances under voluntary license agreements negotiated as provided in subparagraph (A)." And, "In establishing rates and terms for transmissions by eligible nonsubscription services and new subscription services, the copyright arbitration royalty panel shall establish rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller."), https://www.gpo.gov/fdsys/pkg/PLAW-105publ304/pdf/PLAW-105publ304.pdf.

[101] Memorandum Opinion of the Register of Copyrights, Docket Nos. RF 2006-2 and RF 2006-3 (Oct. 20, 2006), 13.

help inform the process of setting PSS rates, they should form an absolute upper bound on such rates.[102]

(131) Even apart from this legislative history, a royalty for PSS based on a CABSAT rate would clearly violate principles embodied in each of the 801(b) policy factors. I evaluate SoundExchange's proposed CABSAT royalty in light of each of the 801(b) policy factors in Section III.D below.

[102] There is support for this conclusion from previous proceedings. In *RIAA v. CRT*, 662 F.2d 1, 12 (D.C. Cir. 1981), the court concluded that a hypothetical marketplace rate would set the upper limit of possible reasonable rates, i.e. an above-market rate can never be a reasonable rate pursuant to Section 801(b). Similarly, in Memorandum Opinion of the Register of Copyrights, Docket Nos. RF 2006-2 and RF 2006-3 (Oct. 20, 2006), 3, the Register concludes that the PSS rate standard "may result in below market rates."

III. Wazzan's analysis of the 801(b) factors is deeply flawed

(132) The previous section presented arguments why Dr. Wazzan's support for the use of CABSAT rates as a benchmark for a PSS sound performance recording royalty rate is inappropriate, including why it is a contravention of each of the 801(b) policy factors. In this section, I show that Dr. Wazzan's analysis of these same factors is also flawed. There are three parts to this analysis. First, I rebut his claim that marketplace rates already *do* account for the 801(b) policy factors. Second, I demonstrate that his conclusion that the 801(b) policy factors are only relevant when accounting for differences between a benchmark and target market is simply incorrect. Third, I rebut his specific arguments regarding (a lack of) adjustments due to the policy factors.

III.A. Marketplace rates *need not* incorporate the 801(b) factors

(133) In his direct report, Dr. Wazzan reports that he has reviewed the expert report of Mr. Jonathan Orszag, "who explains why setting market-based rates is consistent with Section 801(b)(1) objectives one through three," concluding that he agrees with this analysis.[103] Unfortunately, Mr. Orszag's conclusions are simply incorrect – market-based rates ***do not*** necessarily incorporate the 801(b) policy factors - and therefore so is Dr. Wazzan's agreement with them.

(134) In this subsection, I martial arguments demonstrating the flaws in Mr. Orszag and Dr. Wazzan's claims. I begin by summarizing judicial and procedural evidence that concludes, contrary to their claims, that marketplace rates *need not* incorporate the 801(b) policy factors. I then demonstrate how each one of the factors need not be consistent with marketplace outcomes.

III.A.1. Previous rate-setting bodies and the courts have established that marketplace rates do not *necessarily* incorporate the 801(b) factors

(135) Mr. Orszag's arguments, affirmed by Dr. Wazzan, that marketplace rates incorporate the 801(b) policy factors is contrary to the procedural and judicial history of sound recording performance rate-setting. In the very first PSS proceeding, the Librarian of Congress, in an appeal of the determination of the predecessor to the current Copyright Royalty Judges, held that a rate set under the 801(b) policy factors "need not mirror a freely negotiated marketplace rate – and rarely does – because it is a mechanism whereby Congress implements policy considerations which are not normally part of the calculus of a marketplace rate."[104] This view was affirmed by the District of Columbia Circuit Court of Appeals, which concluded "there is no reason to think that the two terms [market rates and

[103] Wazzan WDT, ¶133.

[104] CARP 1998, 63 FR 25,409.

reasonable rates under 801(b)] are coterminous, for it is obvious that a 'market rate' may not be 'reasonable' and vice versa."[105]

III.A.2. Economic analysis supports the conclusion that marketplace rates need not generally satisfy the 801(b) policy factors

III.A.2.a. Overview

(136) While Mr. Orszag's written testimony on whether marketplace rates always satisfy the 801(b) factors is quite brief, his answers to deposition questions reveal more of his thoughts on this matter. In them, he appears to equate marketplace outcomes with economic efficiency.[106] This is unsurprising, as a commonly-held view among economists is that *perfectly competitive* marketplace outcomes indeed promote economic efficiency. In the language of economics, efficient outcomes maximize "total surplus," where total surplus is the sum of producers' (variable) profits and consumers' surplus and consumers' surplus is defined as the difference between what consumers are willing to pay for a product (in the aggregate) and what they actually have to pay. And perfectly competitive markets do yield efficient outcomes.

(137) That being said, Mr. Orszag's conclusions are nonetheless faulty for three reasons. First, he simply makes a mistake. Firms seek to maximize profits and do not necessarily maximize total surplus. If firms have some market power, i.e. if markets are not perfectly competitive, there can be deviations between what they do and that which promotes economic efficiency. In Sections III.A.2 and III.A.4 below, I articulate how these deviations will generally lead to outcomes that do not maximize the availability of creative works and may not lead to outcomes that reflect the relative roles of copyright owners and users with regard to a number of policy factors.

(138) His second error is that the economics literature has lately identified situations where individuals evaluate market outcomes in terms other than just their economic efficiency. For example, it can be the case that markets produce outcomes that people perceive as *unfair*. In Section III.A.3 below, I demonstrate how marketplace rates are *unfair* to PSS providers.

(139) His final error is a presumption that marketplace rates will *always* satisfy the 801(b) policy factors. Even if there was a general presumption that workably competitive marketplace rates satisfied the policy factors, and, as I show in what follows, there is *not* such a presumption, this would not mean that *all* marketplace rates necessarily satisfy the policy factors. One would need to evaluate on a case-by-case basis whether indeed a particular workably competitive rate satisfied a particular policy

[105] *United States Court of Appeals District of Columbia Circuit, Recording Industry Association of America v. Librarian of Congress*, 176 F.3d 528 (D.C. Cir. 1999).

[106] Deposition of Dr. Jonathan Orszag, (Jan. 17, 2017), Tr.335: 18-21; Tr. 340:15-19.

factor. Neither SoundExchange, Mr. Orszag, nor Dr. Wazzan has presented any evidence in this case to evaluate these issues.

III.A.2.b. Marketplace rates will not generally maximize the availability of creative works to the public

(140) With regard to the first factor, Dr. Wazzan summarizes Mr. Orszag's conclusion that "[t]he first policy objective is best served by rates that are sufficiently high to encourage artists and record companies to create new works, but at the same time not so high as to dissuade distributors from undertaking the investments necessary to distribute copyrighted recordings," concluding himself that "market-based rates satisfy these conditions."[107]

(141) This is doubly wrong. First, as acknowledged by Mr. Orszag himself, "[i]f you have a monopoly, then they may not achieve the [801(b) policy] factors here."[108] In other words, a monopolist often seeks to maximize its profit by reducing output, earning more from higher prices paid by those that consume a good at the cost of excluding consumers that value the good at more than its cost but less than its price. As discussed in Section II.D.3 above, however, the CABSAT market used as a benchmark by SoundExchange and supported by Dr. Wazzan and Mr. Orszag reflects just that outcome: it represents a settlement between Sirius XM and a single seller, SoundExchange, rather than agreements between Sirius XM and competing record labels.

(142) Second, the economics literature has long understood that even a *workably competitive* market may not maximize the availability of creative works to the public. In particular, this literature has analyzed the divergence between outcomes provided by the market and those that would be provided by a social planner. The distinction is that the former are those that maximize the *profits* of the firm(s) providing service in the market, whereas the latter maximize *total surplus* in the market, where total surplus is defined as firms' profits plus consumer surplus.[109] Because firms do not account for consumer surplus in their decision-making, but a social planner does, a social planner's decision better reflects outcomes that maximize the availability of creative works *to the public*. As long as firms have *some* market power, i.e. even if the market is workably competitive, if it is not *perfectly* competitive, there will be a divergence between what firms will choose and what a social planner would choose.

(143) There are two reasons for the divergence between outcomes that maximize profit and outcomes that maximize total surplus.[110] The first, and the most relevant for the hypothetical PSS market, is called

[107] Wazzan WDT, ¶20.

[108] Orszag Deposition, 330, lines 18-20.

[109] Consumer surplus is defined as the difference between what consumers are willing to pay for a product and what they have to pay, thus it is a measure of the economic benefit to consumers of having access to a market.

[110] The discussion in this and the next paragraph follows the exposition in Jean Tirole, "Chapter 2: The Profit Maximization Hypothesis" in Industrial Organization, (Massachusetts: The MIT Press, 1988), 35-51.

the *non-appropriability of consumer surplus*. As discussed in Section II.E.1 above, a firm will offer a product only if its variable profits exceed the fixed costs of offering it. But a social planner will offer a product if variable profits *and* consumer surplus exceed the fixed costs. Thus a monopolist will tend to offer *fewer* products than would a social planner.[111]

(144) The second reason for the divergence between outcomes that maximize profits and those that maximize total surplus is due to *business stealing by firms*. The idea is that when an individual firm decides whether or not to offer a product, it considers only *its* variable profits and fixed costs and not the impact its decision has on other firms. Its variable profit comes in part from attracting customers not currently purchasing from any firm, but also customers currently purchasing from rivals. That portion of its profits coming from its rivals is called "business stealing."

(145) By contrast, a social planner accounts for consumer surplus and the *total* of firms' profits. Because a dollar "stolen" from one firm because of the introduction of a new product by another doesn't increase total industry profits (even if it increases the profits of the firm with the new product), a social planner wouldn't count this as a benefit of the new product. Because firms ignore the impact of their decisions on other firms while a social planner doesn't, competitive markets can therefore cause "excessive entry" and offer *more* products than would a social planner.[112]

(146) Whether markets offer too many or too few products is a difficult question to evaluate both in general and in the particular context of markets for music. In media markets, academics have concluded that in the presence of substantial fixed costs, it is possible for markets to induce a "tyranny of the majority": only those products that please the largest group of customers will be offered.[113] In the specific context of music markets, recent research has suggested that the quality of offered music *hasn't* declined since the advent of digital music distribution and that "researchers and policymakers thinking about the strength of copyright protection should supplement their attention to producer surplus with concern for consumer surplus."[114] This is *exactly* the intent of the first 801(b) policy factor.

(147) In my opinion, the PSS market is more likely to suffer from too few rather than too many products. There are now only three major record labels, each with a different (and distinct) portfolio of major artists. Even in a workably competitive hypothetical PSS market, they are sure to have some market

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[111] A. Michael Spence, (1975), Monopoly, Quality, and Regulation, *The Bell Journal of Economics*, 6, (2), 417-429

[112] Michael Spence, "Product Selection, Fixed Costs, and Monopolistic Competition," *The Review of Economic Studies*, Vol. 43, No. 2 (Jun., 1976), pp. 217-235, and N. Gregory Mankiw and Michael D. Whinston, "Free Entry and Social Inefficiency," *The RAND Journal of Economics*, Vol. 17, No. 1 (Spring, 1986), pp. 48-58. An empirical paper analyzing the possibility of overprovision in radio markets is Steven Berry, Joel Waldfogel, "Free Entry and Social Inefficiency in Radio Broadcasting," *Rand Journal of Economics*, Vol. 30, no. 3 (Autumn 1999): 397-420.

[113] Joel Waldfogel, *The Tyranny of the Market: Why you can't always get what you want*, (President and Fellows of Harvard College, 2007).

[114] Joel Waldfogel, 2012. "Copyright Protection, Technological Change, and the Quality of New Products: Evidence from Recorded Music since Napster," *Journal of Law and Economics*, University of Chicago Press, Vol. 55 No. 4, 715–740.

power, raising concerns about the non-appropriability of consumer surplus and the under-provision of products. By contrast, there are few concerns about excessive entry in the hypothetical PSS market. The only firm that has been able to survive over a long period is Music Choice, and, as demonstrated in my direct report, it would only barely do so even at the lower rate I recommend for PSS sound recording royalties. In my opinion, a policy goal of maximizing the availability of creative works would therefore ensure that rates are set in such a way to encourage the production of PSS services.

(148) Dr. Wazzan, summarizing Mr. Orszag, argues that market rates are neither too low to prevent the creation of content and nor too high as to prevent distributors from distributing content, concludes that they therefore encompass this policy factor. But both the first and second halves of this statement are just wrong.

(149) First, as discussed in Section II.E.2 above, a sound recording royalty based on CABSAT rates *would* be too high to prevent distributors from offering a standalone US cable radio service. Thus a CABSAT rate *would* prevent distributors from distributing content. Second, the disconnect between the products produced by markets (i.e. those that maximize profits) and those produced by a social planner (i.e. those that also accounted for consumer benefits) shows that there is no reason to think that a market-based rate will correctly account for consumer benefits. Indeed, as concluded in Section II.E.2 above, a CABSAT-based rate would force the exit of Music Choice, lowering consumer benefits by preventing the viability of the most popular current US cable radio provider, one who particularly focuses attention on making available new music to new audiences.

III.A.2.c. Marketplace rates *are not necessarily fair*

(150) With regard to the second factor, affording a fair return for the copyright owner and a fair income for the copyright user, Dr. Wazzan summarizes Mr. Orszag's conclusion that "'fairness' is satisfied by an outcome that arises through arm's length dealings in the marketplace."[115]

(151) This too is wrong. The past three decades has witnessed a tremendous rise in the study of what economists call "behavioral economics." Behavioral economics applies insights from psychological research into the psychological, social, and emotional factors that influence economic decision-making, in contrast to neo-classical models that assume people make economic decisions based on the rational solution of (sometimes very complicated) optimization problems. In 2002, the psychologist Daniel Kahneman won the Nobel Prize in Economics for his work broadening the dominant neo-classical viewpoint in economics to include such psychological factors.

(152) One feature long studied by behavioral economists is fairness. In a classic article titled "Fairness as a Constraint on Profit Seeking: Entitlements in the Market," Dr. Kahneman, Jack Knetsch, and Richard

[115] Wazzan WDT, ¶20.

Thaler evaluated whether fairness could whether market outcomes are necessarily fair.[116] In a 2000 survey article, Ernst Fehr and Simon Gächter summarized the results of subsequent research on how fairness impacts market outcomes.[117] The insights from this literature that are most relevant to this proceeding can be summarized in what follows.

(153) First, this literature is very clear to define "fair" outcomes as those which provide both buyers and firms with an entitlement to the benefits that would arise in a "reference transaction," where this reference transaction might be based on posted prices or a history of previous transactions between a buyer and firm.[118]

(154) Second, it establishes very clearly that people and firms do not always act as the neoclassical model prescribes: there are situations where firms fail to take advantage of profit opportunities and where people punish firms and/or each other, even when it is costly for them to do so.[119]

(155) Several specific behaviors identified in this research further illuminate how market outcomes do not necessarily provide "a copyright user a fair income" in the PSS market and that a proper adjustment of existing rates for the 801(b) factors would *lower* them for rights users.

(156) First, research has found that "price increases that are not justified by increased costs … are … viewed as unfair."[120] In the context of this proceeding, one can apply this argument to SoundExchange. As there are few if any incremental costs to record labels of serving PSS providers, and whatever costs there may be, there is no evidence in the record that these costs have increased over time. The persistent increase in royalties paid to SoundExchange in the PSS proceedings over time can therefore be considered *unfair*.

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[116] Daniel Kahneman, Jack L. Knetsch, Richard H. Thaler, "Fairness as a Constraint on Profit Seeking: Entitlements in the Market," *The American Economic Review*, Vol. 76 No. 4 (Sept. 1986), 728–741. Hereinafter "KKT."

[117] Fehr, Ernst and Simon Gächter. 2000. "Fairness and Retaliation: The Economics of Reciprocity." *Journal of Economic Perspectives*, 14(3): 159-181.

[118] "The main findings of this research can be summarized by a principle of *dual entitlement*, which governs community standards of fairness: [Buyers] have an entitlement to the terms of [a] reference transaction and firms are entitled to their reference profit. A firm is not allowed to increase its profits by arbitrarily violating the entitlement of [buyers] to the reference price… Market prices, posted prices, and the history of previous transactions between a firm and a transactor can serve as reference transactions. When there is a history of similar transactions between firm and [buyer], the most recent price … will be adopted for reference unless the terms of the previous transaction were explicitly temporary." (KKT, pp 729-30, emphasis in original)

[119] "[T]he rules that govern public perceptions of fairness should identify situations in which some firms will fail to exploit apparent opportunities to increase their profits." (KKT, p729) and, even more strongly, "[P]eople are frequently much nicer and much more cooperative than predicted by [a] self-interest model… People repay gifts and take revenge even in interactions with complete strangers and even if it is costly for them and *yields neither present nor future material rewards.*" (FG, p159, emphasis in original), and also "George Stigler (1981) wrote that when `self-interest and ethical values with wide verbal allegiance are in conflict, much of the time, most of the time in fact, self-interest-theory ... will win.' Our evidence indicates that Stigler's position is often not valid." (FG, p160 citing Stigler, George. 1981. "Economics or Ethics?" In s. McMurrin, ed. Tanner Lectures on Human Values. Cambridge: Cambridge University Press., 176)

[120] KKT, p728.

(157) Second, and by contrast, research has found that a "firm [should] be entitled to its reference profit: [survey respondents] would allow a firm threatened by a reduction of its profit below a positive reference level to pass on the entire loss to its [buyers], without compromising or sharing the pain."[121] In the context of this proceeding, one can apply this argument to Music Choice. As my direct report clearly shows, Music Choice's financial condition has worsened appreciably since the last proceeding and threatens to decline even further. As such, it would be fair to *reduce* the royalty it pays for sound recording performance rights.[122] Similarly, when Music Choice launched, it did so under the expectation that it would have to pay no sound recording performance royalty. Introducing one was therefore *unfair*, and indeed the reason rates for PSS providers were intended to be set according to the second 801(b) factor was to try to accommodate this unfairness.

(158) Third, research has found that "a firm [should] only [be] allowed to protect itself at [a buyer's] expense against losses that pertain *directly to the transaction at hand.* Thus, it is unfair for a landlord to raise the rent on an accommodation to make up for the loss of another source of income."[123] In the context of this proceeding, one can use this argument to further rebut the use of Dr. Wazzan's proposed CABSAT benchmark: it is unfair to demand that a firm serving the PSS market pay royalties that *require* it to earn profits from a secondary market.

III.A.2.d. Marketplace rates *do not necessarily* reflect the relative contributions of owners and users of sound recording performance rights

(159) With regard to the third factor, reflecting the relative roles of the copyright owner and user in a range of contributions, Dr. Wazzan summarizes Mr. Orszag's conclusion that "the third statutory objective is also best satisfied by license fees that reflect marketplace negotiations because such negotiations are likely to reflect the respective contributions of copyright owners and users."[124]

(160) For the same reasons outlined in Section III.A.1 above, this too is incorrect. Just as there is no guarantee that markets, designed to maximize profits, would provide the same set of goods that would a social planner, designed to maximize the sum of profits and consumer welfare, there is similarly no guarantee that market rates – even workably competitive market rates - would necessarily compensate appropriately the relative contributions of copyright owners and users.

(161) In such settings, one must evaluate whether any particular marketplace rate satisfies these objectives based on the evidence presented by the parties in a proceeding. For example, Music Choice's CEO David Del Beccaro has testified how, beginning in 1987, he helped create the entire concept of a digital music service, culminating with the nation-wide expansion of Music Choice as a standalone

[121] KKT, 732.

[122] As discussed in Section IV.A.2 below, since royalty rates are measured as a percentage of revenue, the royalty rate should be lowered when a firm's profitability declines.

[123] KKT, 733.

[124] Wazzan WDT, ¶20.

company in 1991.[125] This *clearly* was a "contribution to the opening of new markets for creative expression" (unmatched by the record labels) that greatly enhanced consumer welfare and therefore a reason to consider setting a PSS royalty different from a marketplace royalty.[126] By contrast, neither Mr. Orszag nor Dr. Wazzan has presented any evidence (1) to support a view that the CABSAT rate is a workably competitive marketplace rate, (2) to adjust for the many meaningful differences between the CABSAT rate and a hypothetical PSS market rate, or (3) that a suitably adjusted CABSAT rate reflects the relative contribution of this or any of the other factors outlined in the third 801(b) objective.

III.B. Wazzan's argument that accounting for the 801(b) policy factors is only relevant to account for differences between a benchmark and target market is erroneous

(162) In his direct report, Dr. Wazzan, citing SDARS I, claims that "The first three [801(b)] objectives address issues that are accounted for in market prices."[127] He further claims, without citations or other support, that "the Judges have held that an adjustment based on these factors is warranted only when the benchmark market and the hypothetical target market under the statutory license are different in ways relevant to these objectives."

(163) As a preliminary matter, even if the Judges had made these claims in SDARS I, they are inconsistent with the appellate precedent described in Section III.A.1 above that concluded both that the policy considerations embodied in the 801(b) factors are not typically embodied in marketplace rates and that marketplace rates may not be "reasonable" in the context of the 801(b) standard. Furthermore, as described in Section II.F.1 above, these statements are also inconsistent with legislative intent: if marketplace rates automatically account for the first three policy factors, there would have been no need for Congress to grandfather PSS providers under the 801(b) standard when it created the willing buyer/willing seller standard. These statements are also inconsistent with sound economic theory, as described at length in Section III.A above.

(164) Putting aside all of these issues, both of these claims are also demonstrably false. In SDARS I, the Judges do *not* conclude that the first three 801(b) policy factors are already accounted for in market prices. Indeed, in their introduction before considering each policy factor in turn, they conclude that "the issue at hand is whether these policy objectives weigh in favor of divergence from the results indicated by the benchmark marketplace evidence [in this case]."[128]

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[125] Del Beccaro WDT, 1-2.

[126] For further arguments in favor of this particular policy factor, *see also* Del Beccaro WDT, pp 43-44.

[127] Wazzan WDT, ¶74, citing SDARS I, 73 FR 4094-5.

[128] In SDARS I, the Judges conclude that "an effective market determines the maximum amount of product availability

(165) The second claim is equally false: if Dr. Wazzan intended his conclusion to rely on evidence from the record in SDARS I, the Judges in that proceeding do *not* conclude that an adjustment based on the 801(b) factors are warranted only when there is a difference between a benchmark and target market. They repeatedly conclude the opposite, for example with regard to the first and second policy factors ("The ultimate question is whether it is necessary to adjust the result indicated by marketplace evidence in order to achieve this policy objective," using identical language) as well as the third ("We find that, considering the record of relevant evidence as a whole, the various subfactors identified in this policy objective may weigh in favor of a discount from the market rate..."). None of these conclusions relate to differences between a benchmark and target market; rather, they relate to whether conclusions about a market rate should be adjusted to account for the non-market factors embodied in the 801(b) provisions.[129]

III.C. Wazzan's specific arguments for adjustments due to the 801(b) policy factors are incorrect

(166) In the balance of his analysis of the 801(b) policy factors, Dr. Wazzan claims to consider whether the differences between the CABSAT market (his proposed benchmark market) and the hypothetical market for PSS sound recording performance rights require adjustments due to the 801(b) policy factors. As discussed in the previous subsection, this is the wrong focus: the issue is whether a market rate, however estimated and if considered by the Judges as possibly informative about a reasonable rate for PSS sound recording performance rights, should be adjusted to account for the 801(b) policy factors. That being said, Dr. Wazzan makes a number of erroneous conclusions in his analysis that merit discussion.

(167) With respect to the first policy factor, "To maximize the availability of creative works to the public", Dr. Wazzan claims, without any factual support, that CABSAT and PSS services appear to provide equivalent availability of creative works.[130] This is a completely unsupported claim. As I discuss in my written direct testimony, Music Choice increases demand for new music and new artists in ways other music services would not.[131]

(168) Furthermore, when AT&T switched from Music Choice to Stingray's CABSAT service in October 2014, the only CABSAT service that competes with Music Choice for new business, many AT&T U-

consistent with the efficient use of resources," but this conclusion is incorrect. To be correct, it would have to instead have said "*a perfectly competitive market* determines the maximum amount of product availability consistent with the efficient use of resources" (emphasis added). As discussed at length in Section III.A.2.b above, markets can very well provide too few products.

[129] Dr. Wazzan is schizophrenic on this topic, as, despite his incorrect conclusions about the role of the 801(b) policy factors in paragraph 74 summarized above, he also (correctly) summarizes their appropriate use in his paragraph 17.

[130] Wazzan WDT, ¶76.

[131] Crawford WDT, ¶¶194-199.

verse customers complained about what they perceived as a lower-quality product. They highlighted important differences between the two services in delivery method,[132] the quality of on-screen information,[133] the availability of music videos, the presence of commercials, the difficulty in the Stingray Music navigating interface, and music availability.[134] They also complained about qualitative differences in the number of genres and the quality of the particular musical selections within genre.[135]

(169) In addition, as documented in the testimony of Mr. Williams, the record industry *pays attention* to Music Choice. They "service" them in an effort to get them to play their artists' music and third-party measurement companies like Mediabase both track and include some of Music Choice's channels on their panels (which impacts how songs are charted and ranked).[136] This shows the recording industry recognizes Music Choice as an important distribution channel for consumers, something that in turn suggests consumers value highly the Music Choice listening experience.[137]

(170) Dr. Wazzan has presented no evidence that CABSAT services like Stingray have these features, certainly not to the same extent as Music Choice. Without them, and if a cable radio service would be viable paying CABSAT rates (as discussed in Section II.C.4, something I think is unlikely), the availability of creative works to the public would decline if a PSS service was replaced by a CABSAT service (as might happen under SoundExchange's proposed rates, particularly if SoundExchange lowered the CABSAT royalty to keep them viable.).

(171) Dr. Wazzan also claims that the lower rates paid by PSS providers relative to CABSAT providers have a negative effect on availability because of opportunity costs to copyright owners.[138] This is remarkably unlikely. Revenues from PSS providers are less than [redacted] of total US music industry revenues.[139] This is miniscule, and even if PSS providers were to pay CABSAT rates, it would still be miniscule. It strains credulity that music industry A&R or marketing decisions would

[132] Music Choice was offered on dedicated channels that allowed consumers to flip from one genre of music to another without any lags, while households had to access Stingray via a portal that downloaded the channel over the consumer's Internet connection. This both required a dedicated Internet connection and prevented instant access to music from different genres.

[133] Music Choice offered information about each song's artist, title, and release year, while Stingray appeared to simply display the CD art from the song's album.

[134] *See* Appendix A.2 with excerpts of the customer reviews and complaints regarding Stingray Music service.

[135] While both Music Choice and Stingray employ expert music programmers, as described in Section II.C.2 above, Stingray's core Canadian cable audio service contains music that American listeners may not value, for example songs by Canadian artists that are unknown in the US and French-language songs. It isn't clear if and how they modify their US channel lineup relative to their Canadian offerings to make them more attractive to an American audience. In his rebuttal testimony, Mr. Del Beccaro describes competition between Music Choice and Stingray and concludes, based on his experience, "we are typically able to keep our affiliates at a higher price than that offered by Stingray because our service is recognized as superior." Del Beccaro WRT, 9.

[136] Williams WDT, 29-34.

[137] Another implication is that there is likely to be a *differential promotional effect* between Music Choice and Stingray.

[138] Wazzan WDT, ¶¶77, 85.

[139] Crawford WDT, ¶26.

change materially with a change in rates in the PSS market. It is certainly the case that neither SoundExchange nor Dr. Wazzan has presented any evidence in support of this claim; indeed industry executives in the last proceeding said just the opposite.[140] This belief is further bolstered by the research I cited in my direct testimony that shows that "the quality of music has increased fairly substantially since 1999," *despite* the major decline in music industry revenues since that time.[141]

(172) With respect to the second policy factor, "To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions," Dr. Wazzan cites the Judges' SDARS I decision which stated that "a fair income is . . . consistent with reasonable market outcome." For the reasons I outline in Section III.A.2 above, I disagree with this conclusion: marketplace rates are *not* inherently fair to PSS providers. Fair rates would not increase despite no increase in SoundExchange's costs, fair rates would decrease in response to Music Choice's declining profitability, and fair rates would not require PSS providers to earn profits from a secondary market in order to pay them.

(173) Dr. Wazzan goes on to conclude that "use of CABSAT and webcasting rates for PSS is consistent with this statutory objective, as the CABSAT and webcasting rates purport to approximate a marketplace rate."[142] While it is not clear why he includes the webcasting rates in these sentences given he is only proposing the CABSAT rate as a benchmark, as I showed in Section II.D.3 above, CABSAT rates are *not* rates that would arise in a workably competitive market. Instead they were negotiated between a monopolist over sound recording performance rights, SoundExchange, and a single entity for whom CABSAT services are a trivial portion of their business, Sirius XM, and for whom the entire service is perceived as a promotional device. Despite there being a willing buyer/willing seller standard for CABSAT services, it is certainly not the case that the Copyright Royalty Judges have ever determined CABSAT rates under that standard, or even reviewed the settlement rates under that standard. They are therefore *not* workably competitive rates.

(174) With respect to the third policy factor, "To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication," Dr. Wazzan concludes that PSS and CABSAT services have similar roles and make similar contributions. This too is demonstrably incorrect. Because CABSAT service providers all earn the majority of their revenue

[140] Mr. Charles Ciongoli, representing Universal Music Group (UMG), "testified that the revenues from Music Choice are not a material revenue source for UMG" and that "UMG does not consider the royalties it receives from Music Choice or from cable radio in general when deciding how many albums to release." *See* Before the Copyright Royalty Judges, Library of Congress, In the Matter of Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services, Docket No. 2011-1 CRB PSS/Satellite II, "Music Choice Proposed Findings of Fact," Sept. 26, 2012, ¶416 citing 6/14/12 Tr. 2165:15-2166:2 (Ciongoli).

[141] Crawford WDT, ¶206.

[142] Wazzan WDT, ¶78.

from other lines of business, they do not have the same cost structures, they do not face the same risk, and they do not incur the same capital investments in the PSS market as the main PSS provider, Music Choice. Furthermore, as described in great detail in Music Choice's CEO David Del Beccaro's testimony, CABSAT providers played nothing like the role that PSS providers did in "opening of new markets for creative expression."[143] As outlined in Section II.F.1 above, it was in part for this very reason that Congress created the PSS category and set the 801(b) policy-based rate standard to determine their rates. Finally, Dr. Wazzan's comparison of Music Choice's expenditure on property and equipment relative to Sirius XM and Pandora during a very narrow period of time is simply misleading.[144] In my direct report, I provided a detailed analysis of Music Choice's financial performance; Exhibit B-3 shows that between 2016 and 2018, Music Choice estimates that it will spend, on average, [redacted] of its VOD-adjusted residential audio service revenue on Programming and Operations and a further [redacted] on Sales and Marketing.

(175) With respect to the fourth and final policy factor, "To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices," Dr. Wazzan makes a number of unjustified claims. First, he claims that "the rate-setting process is intended to generate rates that approach those that would be observed in an unregulated free market."[145] While that may be true for a rate-setting process governed by a willing buyer/willing seller standard, that is not the true for the 801(b) policy standard that applies to the PSS rate. Second, he claims that "Stingray seems to be having some success competing against Music Choice despite paying the higher CABSAT royalties. It is inconsistent with sound competition policy to advantage Music Choice in this competition through a low rate."[146] As discussed further in Section II.C.4 above, it is not at all clear that Stingray will be a viable long-term competitor to Music Choice.[147] More important, though, as I described in Section II.D.3 above, it would be inconsistent with the Judges' mandate in this proceeding to impose a (CABSAT) rate that is the outcome of a negotiation between a monopolist SoundExchange over sound recording performance rights when individual record labels in a workably competitive hypothetical market for such rights would *not* be able to achieve such a rate.

(176) Finally, Dr. Wazzan claims "If the PSS cannot, by some combination of lower profits, higher prices, reduced expenses, or *subsidy from other lines of business* operate their services while paying marketplace prices for the inputs used in their services, the economically-appropriate result is that

[143] Testimony of David Del Beccarro, 36-44.

[144] Wazzan WDT, ¶79.

[145] Wazzan WDT, ¶82.

[146] Wazzan WDT, ¶84.

[147] While Dr. Wazzan discusses each of Stingray, DMX, and Muzak in his arguments, the latter two are not very relevant for outcomes in the US cable radio market. I understand that neither has actively competed for new business for years. I further understand that Mood Music, both firms current corporate parent, is a Canadian company who was very strong in the Canadian market for background music, while both Muzak and DMX were US companies who were strong in the US market for background music. Seeking to expand in the market for background music was very likely the primary reason for Mood Music's decision to purchase both Muzak and DMX.

other providers who can do so (such as the CABSAT services) should be allowed to do so" (emphasis added).[148] This is a fitting conclusion to Dr. Wazzan's faulty analysis as it is so wholly the antithesis of the intent of the 801(b) policy factors. The second 801(b) policy factor states that PSS rates should be set to provide a fair income to the copyright user (in the PSS market). But Dr. Wazzan makes the direct argument for what I believe is an economically unsupportable outcome: that to serve the PSS market, a firm *must* subsidize this market from another line of business. For the reasons discussed in detail above, this would force Music Choice out of business, reducing competition, lowering the quality of cable radio services, and harming consumers, an outcome that is only possible via this proceeding and not through a workably competitive marketplace.

III.D. SoundExchange's Proposed Rates are clearly contrary to the 801(b) policy factors

(177) My analysis in this section to this point has focused on Dr. Wazzan's arguments in support of SoundExchange's proposed rates for PSS sound recording performance rights. In this subsection, I rebut directly these proposed rates as they are themselves clearly contrary to each of the policy factors.

(178) With respect to the first policy factor, "To maximize the availability of creative works to the public", SoundExchange's proposed rates clearly oppose this factor. As described in Section II.E.2.c above, imposing a PSS royalty at the level of the CABSAT royalty would cause the exit of the only active PSS provider in the cable radio market. Furthermore, as described in Section II.C.4 above, there has been no firm that has profitably served this market over the long run paying rates at the CABSAT level (but possibly for Sirius XM, for whom such a service is a promotional device for their satellite radio service). As such, imposing a CABSAT royalty in the PSS market will very likely reduce the availability of creative works to the public.

(179) With respect to the second policy factor, "To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions," SoundExchange's rates equally clearly oppose this factor. By any criteria, a rate which forces Music Choice, the PSS market leader and market participant for 25 years, out of the market due to a rate set in a regulatory process that wouldn't be feasible in a workably competitive market is categorically unfair. By the same token, a rate that increases compensation to record labels despite no extra cost or risk could reasonably considered unfair. This is particularly true given the skyrocketing growth in streaming revenues that have provided record labels with tens of millions of dollars in profit with continued positive growth prospects for the foreseeable future.[149]

[148] Wazzan WDT, ¶86.

[149] As one example, Warner Music Group reported fourth-quarter of 2016 streaming revenues of $311 million, up 47%

(180) SoundExchange's proposed rates are even unfair relative to rates which would be considered by individual record labels. In negotiations with Universal Music Group (UMG) over royalties for Music Choice's music video and VOD products in October 2016, a UMG term sheet [redacted] First, it shows how, in the absence of a workably competitive market (as in the CABSAT market where SoundExchange negotiates on behalf of all the major record labels), SoundExchange can negotiate royalty rates at least [redacted] *times as high* as what an individual record label would accept (cf. Table 3 and the first column of Table 6). Second, it is above the absolute upper bound on what a reasonable royalty rate should be for the PSS market. As demonstrated by the analysis of Music Choice's financial performance under the existing rate, Music Choice could not and would not agree to a rate as high as [redacted] Indeed, that this is just a [redacted]

(181) With respect to the third policy factor, "To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication," SoundExchange has presented no compelling evidence in support of a view that its enormous rate increase could be justified based on any changes in the relative contributions of the record companies with respect to these various sub-factors. By contrast, Mr. Del Beccaro outlines at great length the role played by Music Choice relative to the record labels in each of these factors.[151] If the judges choose to adjust a PSS rate, however determined, based on this factor, it could only be in the favor of Music Choice.

(182) With respect to the fourth and final policy factor, "To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices," there can be no doubt that SoundExchange's proposed rate would be disruptive. As described in Section II.E.2 above, it would necessitate the exit of Music Choice with no ready replacement. Music Choice would lose and consumers would lose. Even SoundExchange would lose, as it would see that no firm can be viable at such a royalty, with consequent losses in PSS revenue (albeit modest) as well as the promotional

from the same period in 2015. Ed Christman, "Warner Music Reports Solid Growth of Streaming, Publishing Revenue in Quarterly Earnings," Billboard, Feb. 7, 2017. http://www.billboard.com/articles/business/7684894/warner-music-group-q1-earnings-results-wmg. In the same article, WMG CEO Steve Cooper noted, "As an industry, we have only fulfilled a fraction of the streaming model's long-term potential." Global subscribers to paid music services reached 100 million, but he concluded "that's only one percent of the world's population; it's just a drop in the bucket," with the article further noting that "this is why he is upbeat about continued growth for the music industry."

[150] UMG Recordings Servies, Inc. ("UMG") and Music Choice ("COMPANY") Term Sheet Proposal - October 2016.

[151] Del Beccarro WRT, 19-46.

effects that a PSS service has on other sources of record label revenue (discussed in Section V.A.3 below).

(183) Whether evaluating SoundExchange's rate proposal *or* Dr. Wazzan's arguments in favor of it, it is evident that a CABSAT rate would be diametrically opposed to the goals advanced by the 801(b) policy factors.

IV. Wazzan makes a number of additional incorrect and/or unjust claims

(184) While the main thrust of Dr. Wazzan's arguments center on his proposal of the CABSAT rate as a benchmark for the hypothetical PSS market for sound recording performance rights and the (lack of) adjustment in those rates to account for the 801(b) factors, he makes a number of other incorrect and/or unjust claims in his report. I address three here: his support for SoundExchange's proposed per-subscriber rate instead of the share of revenue rate that has historically been set for PSS sound recording performance royalties, as well as for its increase over time, his claim that Music Choice does not pay its cable company partners arm's-length rates, and his proposal that Internet streaming of Music Choice's channels should be paid separately from, and in addition to, the PSS rate.

IV.A. A percentage-of-revenue rate is superior to a per-subscriber rate and shouldn't increase over time

IV.A.1. A percentage-of-revenue rate is superior to a per-subscriber rate for compensating rightsholders

(185) In his testimony, Dr. Wazzan writes that he supports SoundExchange's proposal for a per-subscriber royalty for PSS sound recording performance rights. He offers no discussion or analysis of why such a rate should be preferred to the percentage-of-revenue rate that has long been used for such rights. As such, there is no direct analysis to rebut. That being said, it is my opinion that a percentage-of-revenue rate structure is superior to a per-subscriber rate structure for PSS royalties.

(186) The primary advantage of a percentage-of-revenue rate structure is its *flexibility*. Anything that increases demand for a rights user's service will be reflected in greater revenue and therefore greater royalties to rightsholder. Similarly, anything that decreases demand will be reflected in lower revenues and lower royalties. Both rights users and rightsholders gain or lose in proportion to the value created by the rights.

(187) A per-subscriber rate introduces both inflexibility and risk and requires more detailed information in setting an appropriate rate. It introduces inflexibility as rates for PSS sound recording performance rights are decided once every five years, so any decision, whatever its level, cannot respond to changes in market conditions between rate cases. Furthermore, while for reasons I discuss below I think it is particularly warranted in this case, the Judges have not retroactively corrected for royalties that may have been too high or too low based on mistaken predictions of future market conditions. Thus any mistakes, whatever their direction, are likely to be permanent under a per-subscriber rate structure.

(188) A per-subscriber rate also introduces risk to rights users as they are liable for such payments regardless of how their market changes over time. In good times, this is good for them, but in bad times it poses a difficult problem, particularly in the PSS market where royalties are a significant share of firms' expenses and too large a royalty bill can have an adverse effect on a firm's viability.

(189) Not only is a share-of-revenue royalty preferred to a per-subscriber royalty that rises over time, it is also preferred to a per-subscriber royalty that is constant over time. Music Choice, the largest PSS provider, has faced declining per-subscriber rates from MVPD affiliates for years.[152] In such a setting, a constant per-subscriber royalty implies an *increasing* share-of-revenue royalty. Thus, *if* a per-subscriber royalty was to be introduced, only a *declining* per-subscriber royalty would make sense.

(190) Introducing a per-subscriber rate structure would also create a significant administrative burden. All parties in the proceeding would need to present evidence for how they anticipate the market to evolve and justify patterns of either rising or falling rates. These would necessarily be speculative, introducing uncertainty into the rate process.[153]

(191) The Copyright Royalty Judges have previously recognized that a percentage of revenue rate structure is appropriate for the PSS. The PSS have paid a fee based on a percentage of revenue since 1998 when the initial PSS royalty rates were established.[154] At that time, the percentage-of-revenue structure was adopted over a per-performance one due to "intractable problems associated with measuring usage and listenership to performances of sound recordings."[155] Given the advantages outlined above, the Judges should continue to prefer such a rate structure over a per-subscriber structure as well.

IV.A.2. A percentage-of-revenue royalty rate should *not* increase over time

(192) Even if one agrees that a percentage-of-revenue royalty rate is appropriate, there is the issue of whether that rate should automatically increase or decrease during the rate period. In the previous

[152] Testimony of David J. Del Beccaro, 22-23. ("By 1996, Music Choice averaged only [redacted] per customer per month for its residential audio service. By the time of the SDARS II proceeding, this number was down to [[seven cents]] per customer. Since SDARS II, this downward pressure had continued. The average price for the [redacted] largest MVPDs, which make up [redacted] of our total subscriber base, is now [redacted] per customer. Just three years ago, the average price for [redacted] of our subscriber base was [redacted] per subscriber. That is a [redacted] reduction in just the past three years.")

[153] One reason for adopting a per-subscriber rate for webcasters is that I understand that there have been instances where webcasters under-report revenue, exploiting this feature of a percentage-of-revenue rate. This is not an issue in the PSS market, where all PSS rate-payers, and especially the largest, Music Choice, have long histories of accurately reporting revenues in a percentage-of-revenue system.

[154] Library of Congress , Copyright Royalty Board, 37 CFR Part 382, [Docket No. 2011–1 CRB PSS/Satellite II], Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services. FR 23056. Hereinafter SDARS II.

[155] SDARS II, 78 FR 23056.

proceeding, when weighing the second 801(b) policy factor (fair income/fair return), the Judges concluded that additional performances embodied in Music Choice's proposed increase in channel capacity merited an 1% increase in the royalty rate for the year 2014-2017.

(193) This appears to have been a logical error. As discussed above, anything that increases demand for a rights user's service (e.g., an increase in the number of channels that results in an increase in the number of performances), will naturally be reflected in the revenue it receives for its service. If such an increase in revenue materializes, then there will be a consequent increase in the royalty paid to the rightsholder, *without* a change in the royalty rate. This is even true when accounting for inflation, as inflation will influence a rights users' revenue and thus the royalties paid.[156] Conversely, if the increased channels do not provide sufficient value to generate increased revenue, there is no sound justification for an increase in royalty payments to SoundExchange.

(194) This issue is particularly salient for Music Choice, as its large planned expansion in the number of audio music channels at the time of the last rate proceeding did not materialize and they experienced no increase in households' listening time.[157] As such, it paid a greater share of royalties to rightsholders in the years covered by the last rate proceeding *without* a consequent increase in the number of performances.

(195) In this proceeding, SoundExchange has proposed that the CABSAT rates (which are only known through 2020) increase at a 3% rate for 2021 and 2022. Neither they, nor Dr. Wazzan, however, has provided any theoretical or empirical support for this proposal. As described in the previous subsection, if a per-subscriber royalty were to be chosen, the only reasonable one would be a decreasing one. And if a share-of-revenue royalty were to be chosen, a constant share-of-revenue royalty will automatically increase or decrease payments to rightsholders in response to changes in a rights user's economic environment.

(196) Indeed, using the bargaining framework put forward in my direct report, one can argue that a share-of-revenue royalty *could* change according to the size of the negotiating parties' joint surplus over the projected period. As Music Choice's financial condition has worsened in the past several years, this would rationalize a *decreasing* share-of-revenue royalty.[158]

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[156] Note that the situation is different for a per-subscriber rate, for which it might make sense to include an inflation adjustment across years. I understand that Music Choice's affiliate agreements are themselves adjusted for inflation on an annual basis. *See* Del Beccaro WRT, 21.

[157] Crawford WDT, ¶213

[158] If rates could be established as a share of *profits*, then there would be no need to change the rate as a rights users financial condition worsened. Because rates are a share of revenue, however, then declining profitability should be associated with a declining share-of-revenue rate.

(197) In the most recent Web IV proceeding, the Judges considered whether a per-performance rate should automatically increase with time (but for an inflation adjustment) and concluded that it should not.[159] Similarly here: there should be no presumption of an increasing royalty rate "baked in" to the rate-setting process.

IV.B. Music Choice's cable company partners pay arm's-length rates for the Music Choice service

(198) In his direct report, Dr. Wazzan concluded that "Music Choice is majority owned by cable companies … and it charges lower rates to these providers. And that while some of these partners are larger cable companies, these fees do not appear to be the result of charging lower rates to cable companies with greater numbers of subscribers, as shown in [Wazzan's Table 1]. Thus, it is not clear that the partner prices are the result of arms-length marketplace transactions."[160]

(199) In addition to making a number of factual errors in his premises, Wazzan's arguments are also unfounded. From a factual perspective, Time Warner Cable has far more subscribers than the [redacted] million reported in his Table 1 and Cox Cable has far fewer than the reported [redacted] million.[161] More problematic is the factual error to claim that Music Choice is majority owned by cable companies including Comcast, Cox, and Time Warner Cable. The document he cites in support of this claim simply list MC shareholders with their voting and non-voting shares; Dr. Wazzan does not specify how he reached the conclusion that Music Choice is majority-owned by cable operators. In fact, Music Choice's cable company part-owners *in total* represent only [redacted] of the total equity and [redacted] voting share in the firm, each of whom itself has a comparably smaller share.[162]

(200) This second error is itself sufficient to refute Dr. Wazzan's claim that Music Choice doesn't negotiate arms-length terms with its cable industry partners. In Music Choice CEO David Del Beccaro's direct

[159] The Judges rejected the increase in the per-subscriber rate proposed by SoundExchange's expert, Dr. Daniel Rubinfeld, because (1) Sound Exchange failed to make a factual showing for the increase, (2) Dr. Rubinfeld acknowledged that his opinion was neither based on theory nor empirical analysis, and (3) benchmark agreements were not helpful as some have escalators and others do not. Furthermore, the Judges stated that markets could move in either direction or stay constant in the future, so the impact on the rates could not be predicted (Web IV, 26351-26352). They did allow for an inflation adjustment, but this is reasonable for a per-subscriber rate (though not for a percentage-of-revenue rate).

[160] Wazzan WDT, ¶91. He makes this argument in the context of motivating why SoundExchange's proposed per-subscriber rate is more appropriate than a percent-of-revenue rate. As I show in what follows, because his arguments regarding Music Choice providing preferential rates to part-owner cable operators are unfounded, this also rebuts his argument in favor of a per-subscriber rate instead of a percent-of-revenue rate.

[161] It would appear he mistook the identities for each in his table. In December 2016, Time Warner Cable/Spectrum had [redacted] million digital subscribers and Cox Communications had [redacted] million digital subscribers. (Music Choice subscriber data).

[162] Music Choice CEO David Del Beccaro testified that "no single partner holds a controlling interest in Music Choice and, in fact, as a group the non-cable partners hold a significantly greater ownership interest (by a two to one margin) in Music Choice than our cable partners do as a group" (*See* Del Beccaro WDT, 2). *See* Del Beccaro WRT, 16]. The cable company partners' equity and voting ownership is as follows: [redacted]

testimony, he speaks at length about how the deals done with their partners have been conducted at arm's length (for both cable company *and* record company partners) and how some of the most protracted and difficult negotiations have been with their cable company partners.[163]

(201) This isn't surprising. The cable company with the largest (voting) ownership stake in Music Choice is [redacted].[164] Why would Music Choice's other owners agree to a "sweetheart" deal with Cox if it reduced the value of the company? And why would Music Choice's management provide a benefit to one partner to the detriment of all the other partners (cable and non-cable) and the company itself? Even if all of Music Choice's cable operator partners were willing to go along with lower rates for cable industry partners on a *quid pro quo* basis, their total ownership stake is less than [redacted] of Music Choice's owners, or Music Choice's management, acting on their behalf, to object and prevent it from happening.

(202) Furthermore, the patterns of cable company rates reported in Dr. Wazzan's Table 1 are perfectly consistent with the widespread practice of providing quantity discounts to the largest cable companies by owners of content distributed on cable systems.

(203) Indeed, comparing in Dr. Wazzan's Table 1 a simple ranking of cable companies by size with the rates they pay to Music Choice shows that the largest operators (Comcast and Time Warner Cable) pay the lowest rate and the smallest operator (CSC Holdings, Inc., the parent company of Cablevision Systems) pays the highest rate.

(204) Between these extremes are only two deviations from a pattern of lower rates for bigger operators, and each easily can be explained. First, [[[redacted][166]]]

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[163] David Del Beccarro WDT, 2.

[164] Del Beccarro WRT, 16. MC0003241, SX Ex. 019. *See also* MC000321, MC000230.

[165] Kagan data. *See also* Ken Belson, "Verizon begins competing for Cable TV Customers," The New York Times, July 28, 2008. http://www nytimes.com/2008/07/28/nyregion/28verizon html.

[166] Time Warner Cable, whose contract with Music Choice started on [redacted] and Comcast, whose contract with Music Choice started on [redacted] were among the largest cable providers in the US at the time these were signed (SNL Kagan data). *See also* Comcast Press Release, "Comcast Provides Financial Outlook for 2004," Feb. 11, 2014. http://corporate.comcast.com/news-information/news-feed/comcast-provides-financial-outlook-for-2004. ("The Company is the largest cable company in the United States, serving over 21 million cable subscribers."); Cox News

(205) Further evidence confirming this relationship between the rate Music Choice has been able to negotiate and the size of the MVPD affiliate is available in Mr. Del Beccaro's rebuttal testimony. There he describes how, [redacted].[167] The reason? DirecTV had more subscribers at the time.

(206) In the previous proceeding, SoundExchange's expert, Dr. Ford, also raised the question whether Music Choice's contracts with its cable partners reflected arm's-length transactions, advancing the exact same arguments as Dr. Wazzan, and those arguments were summarily dismissed.[168] Dr. Wazzan's arguments making the same claims should also be disregarded.

IV.C. Fees for Internet Transmissions to PSS Subscribers must necessarily be part of, and included within, the PSS rate

IV.C.1. There are important defects in SoundExchange's proposal that PSS providers should pay for Internet transmissions to PSS subscribers

(207) As a preliminary matter, I point out two important defects in SoundExchange's proposal that PSS providers should pay for Internet transmissions to PSS subscribers. The first is a logical inconsistency. SoundExchange has proposed the CABSAT rate as a benchmark for the PSS sound recording performance royalty, but claims that Stingray, a CABSAT rate-payer, [redacted].[169] It is not clear how this is possible. I understand that portions of Stingray's AT&T U-

Release, "Cox Communications Announces Third Quarter and Year-to-Date Financial Results for 2005," Sept. 30, 2005. http://newsroom.cox.com/news-releases?item=175. ("The nation's third-largest cable television provider, Cox offers both analog cable television under the Cox Cable brand as well as advanced digital video service under the Cox Digital Cable brand.") As described in Mr. Del Beccaro's rebuttal testimony, while affiliate size is the most important factor in rate negotiations, other factors like the length of a commitment on the part of an affiliate of the extent to which they are willing to take all of Music Choice's product offerings can also impact a negotiated rate [redacted] *See* Del Beccaro WRT, 16-19.

[167] Del Beccaro, WRT, 18.

[168] "It is not surprising that the partner cable operators, which are in most instances of greater size with respect to numbers of subscribers than the nonpartner licensors of Music Choice's service, would be able to negotiate lower per-subscriber licensing fees due to their ability to deliver more subscribers to the service. Further, the cable partners represent only a third of Music Choice ownership, and do not appear to be able to influence rates any more than Music Choice's record company partners, who own one quarter of the company. 6/11/12 Tr. 1454:16-22 (Del Beccaro). SoundExchange's "Non Arm's Length Transaction" adjustment is founded upon inference and speculation and is not supported by the record evidence." SDARS II, 78 FR 23061.

[169] [In the Matter of: Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services, Docket No. 16-CRB-0001 SR/PSSR (208-2022), SoundExchange's Surreply in Opposition to Music Choice's Motion to Compel SoundExchange to Produce Documents and CABSAT Settlement Documents (Jan. 27, 2017), 3 and Exhibit A: Declaration of Brieanne Jackson (On behalf of SoundExchange). *See* Appendix E: Stingray webcasting activities documents. *See* also I understand that Music Choice's affiliate agreements

verse service, which it took over in October 2014, is delivered via an "app" using Internet Protocol technology.[170] Similarly, I understand that consumers can access Stingray Music via apps on mobile phones and tablets. And a current screenshot of Stingray's US homepage advertises "Listen to free music on TV, *mobile, and the web*" (emphasis added), with "Unlimited, ad-free online streaming of music channels in all popular genres."[171]

(208) For SoundExchange's position to be logically consistent, it must be the case that both of these services are webcasting services for which Stingray should pay royalties *or* that these services are not webcasting services for which Stingray should pay royalties. As Stingray has not paid royalties, the first one can't be true. In which case, the second one must be, so how can SoundExchange presume to ask PSS providers to pay royalties for similar services?

(209) The second is an incomplete analysis. Even if the Judges were to decide that PSS providers should pay for Internet transmission of a PSS service, and, as I show in the next subsection, there is *not* such a presumption, SoundExchange and Dr. Wazzan have proposed PSS providers pay using the rates paid by non-interactive webcasters, *without accounting for the many differences between the two services*, including having different buyers competing in different markets, different modes of use, different cost structures, and different demand characteristics. Dr. Wazzan nominally knows how to conduct a benchmark analysis and has completely failed to do so in this case.

IV.C.2. Sound Exchange has long accepted that web distribution of PSS services is included within the PSS rate for sound legal and economic reasons

(210) Putting aside these preliminary matters, in his direct report, Dr. Wazzan writes that, "as an economic matter, I believe that Music Choice's Internet streaming should be valued separately from its television-based service."[172] Based on this belief, he further concludes that "the Part 380 (Non-interactive Webcasting) rates that would be paid for Internet streaming ancillary to such a service must provide a reasonable approximation of a market royalty for Internet streaming ancillary to the core PSS television-based service."[173]

(211) This analysis is faulty for several reasons. First, Music Choice has been providing audio channels to its subscribers via the Internet as part of its residential audio service since 1996, a fact well known to SoundExchange. When it announced the introduction of some new features to its Internet transmissions, Music Choice and the RIAA, SoundExchange's parent company before it became an independent entity, exchanged four letters over several months, discussing exactly whether Internet

are themselves adjusted for inflation. *See* Del Beccaro WRT, 21.

[170] Del Beccaro WRT, 33-34.

[171] *See* Appendix A.1 Stingray Music US website.

[172] Wazzan WDT, ¶70.

[173] Wazzan WDT, ¶73.

transmission of its existing audio channels required separate rights payments.[174] The RIAA initially said that it did and Music Choice said that it did not. This discussion continued into June of 2005 when, after Music Choice's second letter denying the RIAA's request and providing the reasons for their denial, the RIAA dropped the matter.

(212) Given this history, it is surprising that SoundExchange has revisited this point. As pointed out to them in a letter from Music Choice on June 30, 2005, the Conference Committee report on the DMCA expressly permits Internet transmission of pre-existing audio services, writing "[I]f a cable subscription music service making transmissions on July 31, 1998, were to offer the same music service through the Internet, then such Internet service would be considered part of a preexisting subscription service."[175] It is even more surprising that SoundExchange brings it up in this rate proceeding, as Music Choice has offered such a service over the years covered by all of the previous rate proceedings (years which included one audit by SoundExchange) without any controversy over Music Choice's consistent position that its PSS royalty payments covered transmissions made through the internet.

(213) Putting aside the validity of raising this issue after so many years of SoundExchange's acquiescence to Music Choice's position, Dr. Wazzan's argument should be rejected. First, as a preliminary matter, the non-interactive webcasting rate is based on a willing buyer/willing seller standard and not the policy-based 801(b) standard set for PSS. Second, on technical grounds, I understand that Music Choice does not have the data necessary to track individual performances and pay a per-performance rate like that asked by SoundExchange and that, even if it were appropriate – which it is not – it is just not implementable as a practical matter.

(214) More important by far, however, is that a separate rate for the Internet retransmission of PSS audio channels is unsupportable on both legal and economic grounds. As described above, Congress *expressly included* Internet retransmission as part of the PSS designation when it passed the DMCA.

(215) Against this, Dr. Wazzan argues that, much as he thinks CABSAT rates can and should be used as a benchmark for a PSS rate, he also thinks the rules for the Internet transmission of CABSAT services should also be applied to the PSS. The regulations applicable to CABSAT providers, he notes, clearly indicate that the CABSAT license (and rate) is "limited to a service `transmitted to residential

[174] *See* Appendix C. SoundExchange and RIAA correspondence.

[175] DMCA (Digital Millennium Copyright Act) Conference Report, 89. (Oct. 8, 1998). https://www.copyright.gov/legislation/hr2281.pdf. This understanding was confirmed by the Register of Copyrights in the 2006 PSS proceeding, where they concluded "it is clear why a service would seek to be classified as a preexisting subscription service for the purposes of §114. A designation as a preexisting subscription means that the service will pay royalty fees that are set according a standard that may result in below market rates and it has the added benefit that the service makes its offerings of subscription transmissions in a new medium without losing the status as a preexisting service. The legislative history construing the statutory framework that provides for these services also makes clear that these benefits are limited to only a handful of services that were in operation on July 31, 1998." (Memorandum Opinion of the Register of Copyrights, Docket Nos. RF 2006-2 and RF 2006-3 (Oct. 20, 2006), 5).

subscribers of a television service' through an MVPD using 'a technology that is incapable of tracking the individual sound recordings received by any particular consumer.'"[176]

(216) But Dr. Wazzan's proposal to impose the scope limitations of the CABSAT regulations onto the PSS suffers from the same flaws as his proposal to use the CABSAT market as a benchmark for rates! The scope limitation of the CABSAT license quoted by Dr. Wazzan does not come from the Copyright Act or from a decision by the Copyright Royalty Judges. In a workably competitive marketplace agreement, or in a rate determination by the Judges based on a similar standard, ancillary internet transmissions could, and likely would, be included as a bundled part of a CABSAT rate. The exclusion of such transmissions cited by Dr. Wazzan only exists in the CABSAT regulations as a result of the settlement between SoundExchange and Sirius XM.

(217) For the reasons discussed above, that settlement is simply unreliable as a marketplace benchmark, particularly as the settlement itself expressly prohibits using the CABSAT rates *or terms* as benchmarks in this rate proceeding. But using the CABSAT settlement agreement as a benchmark for this limitation on the scope of the license is even more inappropriate than using it for the rate. As discussed in the rebuttal testimony of Mr. Del Beccaro, Sirius XM does *not* include Internet or mobile app access as part of its DISH network services.[177] As such, this settlement term doesn't even apply to them! Consequently, Sirius XM's acquiescence to this regulatory restriction tells one nothing useful about whether such a restriction would arise in a workably competitive CABSAT marketplace. Putting aside that the legislative history of the PSS rate specifically allows for Internet transmission of PSS services, this background clearly shows that terms about webcasting in CABSAT rates should absolutely not be taken as informative of appropriate rules for PSS services.

(218) Notwithstanding all of the arguments raised to this point, there are also no economic grounds for charging a separate rate for Internet retransmission of PSS services. Including Internet retransmission of Music Choice's audio channels as part of the service increases the value of the service, and thus the value of the digital cable bundle to which households subscribe in order to get access to Music Choice. This value is likely to be well understood by cable operators and factored both into their decisions to reach affiliation agreements with Music Choice and their negotiations regarding the rate they are willing to pay for such affiliation. Thus any value provided to households from the Internet retransmission of Music Choice's audio channels *will already be included in the percent-of-revenue rate* structure that has always been used to set sound recording performance royalties for PSS.

(219) Furthermore, the Internet distribution of PSS audio channels only allows *existing subscribers of PSS services* to access them over the web. I understand that such patterns are common in the television industry.[178] Which makes sense: households are *already paying* for PSS services and PSS providers

[176] Wazzan WDT, 29.

[177] Del Beccaro WRT, 3-4.

[178] Del Beccaro WRT, 27-28.

are already paying SoundExchange for their access. To make PSS providers pay again for such households would simply double-charge them, over-compensating rightsholders. By contrast, for genuine Internet webcasters, the Internet is the *only* way customers can access music. In this case, of course it is reasonable for SoundExchange to demand royalties. But not for the rebroadcast of PSS channels over the Internet.

(220) Given the body of evidence discussed above, there is no reason, economic or otherwise, to specifically split out Internet retransmissions from the PSS rate. The Judges should therefore reject SoundExchange's and Dr. Wazzan's arguments that they should be.

V. Ford rebuttal

(221) Counsel for Music Choice also asked me also to evaluate Dr. George Ford's arguments evaluating the potential for promotional or substitutional effects of PSS with other music services as well as the implications of the profitability of alternative services on PSS royalties if indeed PSS have a promotional effect.

V.A. Dr. Ford provides no evidence of cross-platform substitutability and the importance of music discovery strongly suggests cross-platform promotional effects

V.A.1. Summary of Dr. Ford's arguments

(222) Throughout his report, Dr. Ford argues that PSS services are substitutable with and do not therefore promote other services that are more profitable to rightsholders (e.g. subscription webcasting).[179] He concludes "I believe that the Copyright Royalty Judges can safely and responsibly ignore any proposed adjustment to a benchmark rate to account for relative promotional effects for the permanent copy platform. To the extent that this issue affects the Judges' consideration, such attention should be focused on platform substitution, not relative promotion."[180]

(223) Given that the entire purpose of Dr. Ford's expert report is to opine about the potential promotional effects of PSS services, it is disappointing that *he provides no empirical evidence one way or another to evaluate such effects.* The extent of his evidence is to note that "a listener can only listen to one song at a time," to cite the recent Web IV decision that did not provide a promotional discount to the rates set for non-interactive webcasters, to cite conclusions from that proceeding that interactive and non-interactive *could* be substitutable (emphasis added), to point out that Sirius XM themselves claim they substitute with other music services, and to note the views of music industry executives that services are substitutable.[181] *None* of these remotely qualify as convincing evidence.

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[179] "Music services and platforms compete with one another for attention and/or subscription dollars of listeners," (Ford WDT, p8), "Music services and platforms, are, in large part, substitutes for each other," (Ford WDT, 18), and "[T]o the extent that any service, including Sirius XM or the PSS, seeks a discount for its purported promotional effects, the analysis should focus on how the service drives sales of [subscription and ad-supported] distribution platforms. Such a claim would be extremely difficult to support, however, as these modern distribution platforms are more likely to be substitutes than complements." (Ford WDT, 13)

[180] Ford WDT, 4.

[181] Ford WDT, 10, Ford WDT, 2-3, "the availability of non-interactive services could cause listeners to substitute non-interactive listening at the expense of interactive listening" (Ford WDT, 8, FN 25, *citing* Web IV, 81 FR 26327), "As Sirius XM's own documents bear out, the most popular and growing music platforms 'compete directly with [Sirius XM's] services.'" (Ford WDT, 12-13, FN 47, citing Sirius XM's 2015 Form 10-K), "Thus, substitution across various platforms, some paying hugely different royalties, is what the industry experts, such as SoundExchange witnesses Kushner and Harrison, believe to be the dominant consideration in the modern music marketplace." (Ford WDT, 10)

V.A.2. None of Dr. Ford's "evidence" is convincing

(224) Some of this evidence can quickly be rebutted. From a narrow perspective, Sirius XM's 10-K filing quoted by Dr. Ford speaks only to the competition between their service and "Internet Radio and Internet-Enabled Smartphones" and not the subscription services (e.g. interactive webcasting) implied by Dr. Ford's use of the quote.[182] Even so, Sirius XM does list other services from which consumers can obtain content, including terrestrial radio stations, Internet radio stations, and Internet streaming services.

(225) Even if music platforms generally "compete," however, that *doesn't* necessarily mean that they are substitutes and not complements from an economic perspective.[183] Dr. Ford notes that "music is consumed one service and one platform at a time, so the platforms and services are inherently substitutional in this regard. When the same song is played on Spotify, Pandora, Sirius XM, terrestrial radio, or Music Choice, the song is consumed exclusively on that platform at the loss of another…"[184] From this, he concludes services are necessarily substitutes.

(226) This is a ridiculously simplistic view of the world. While it is true that a consumer can only listen to only one song on any one service at any one moment of time, people purchase services to use over much longer time horizons, can (and do) purchase multiple services (as I show in the next sub-section), and can (and do) regularly switch between them according to their needs or preferences. Thus while substitutes *at any given instant*, this does *not* mean that services must necessarily be substitutes from an economic perspective.

(227) Indeed, Dr. Ford's first citation of the Web IV decision, if anything, supports the view that services are certainly *not* substitutable (and indeed might be complementary). In their review of the evidence put forward by both SoundExchange and the Parties in the Web IV decision, the Judges wrote favorably of the survey evidence of Mr. Larry Rosin (President of Edison Research), an expert survey witness for Pandora. He was retained to evaluate "whether on-demand services and non-interactive services are substitutes or complementary products." In their Web IV decision, the Judges found

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[182] Sirius XM 10-K at 5 with respect to the quote by Dr. Ford states "Internet Radio and Internet-Enabled Smartphones. Internet radio services often have no geographic limitations and provide listeners with radio programming from across the country and around the world. Major media companies and online providers, including Apple, Google Play, Pandora and iHeartRadio, make high fidelity digital streams available through the Internet for free or, in some cases, for less than the cost of a satellite radio subscription. These services compete directly with our services, at home, in vehicles, and wherever audio entertainment is consumed."

[183] A product A is an economic substitute for a product B if demand for product A goes up when the price increases for product B. This is called a positive cross-price effect. A product A is an economic complement for a product B if the demand for product A goes down then the price increases for product B. This is called a negative cross-price effect. Cross-price effects are often measured as an "elasticity", defined as the percentage change in the quantity sold of product A for a given percentage change in the price of product B. Substitutes have positive cross-price elasticities and complements have negative cross-price elasticities.

[184] Ford WDT, p18.

"Mr. Rosin's random survey to be generally credible," rejecting SoundExchange's criticisms of it (emphasis removed).[185]

(228) In evaluating the relevance of Mr. Rosin's conclusions for this proceeding, I associate findings applying to non-Interactive Internet radio services like Pandora as being the most likely to also apply to cable radio services provided by PSS providers due to their *relative* similarity, i.e. both are "lean-back" services and share more characteristics than does either with "lean-in" interactive services. In Section V.A.3.b below, I provide a model of music discovery and consumption that justifies this assumption.

(229) Mr. Rosin makes several findings that are of potential interest and contrary to Dr. Ford's claims. First, he concludes that "noninteractive services like Pandora and iHeart are not close substitutes for interactive on-demand services such as Spotify." He does so based on survey results that show only 9% of Internet audio users would switch to an on-demand Internet music service if all free Internet radio or music services no longer existed.[186] I agree with his conclusion that this suggests very limited substitutability between on-demand and non-interactive services.[187]

(230) Another valuable insight in the Rosin study not highlighted by the Judges in Web IV is also relevant. The answer to the same question shows that substitution away from a lean-back service like Internet radio is *far* more to other free music services than to paid, on-demand services: 34% would listen to terrestrial radio, 24% would listen to their existing CDs or downloads, 16% would watch and listen to music videos on YouTube or Vevo, and 15% would simply listen to less music.[188]

(231) Similarly the other way: when asking existing Pandora users from where their time spent listening to Pandora replaced, 46% said it was new listening time not taken from other sources of audio listening, 23% was drawn from time previously spent listening to terrestrial radio, 18% was drawn from their existing CDs or downloads, 7% was drawn from other non-interactive services, and *only 1% was drawn from an on-demand service like Spotify or Rhapsody.*[189] Not only are lean-in services like Spotify *not* substitutes for lean-back services like Internet and Music Choice, what *are* substitutes are other sources of lean-back listening or simply not listening to music at all.

(232) One can also disregard Dr. Ford's latter citation of the Web IV decision. That services *could* be substitutable does not mean that they *necessarily* are substitutable. They could equally well be

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[185] Web IV, 81 FR 26328.

[186] Rosin WRT, Figure 10.

[187] Unfortunately, this question, while useful for evaluating substitutability, is less useful for addressing complementarity. Strategy documents from Warner Music Group show that they believe that free services [redacted] an effect that would be unlikely to be revealed in a one-time survey response. Warner Music Group, "Digital Strategy," Nov. 15, 2012, SX Ex. 011 (SoundX_000076302-330), 20.

[188] Rosin WRT, Figure 10.

[189] Rosin WRT, Figure 11.

complementary. Similarly, one can also disregard his claims of support from industry executives. Industry executives have every incentive to articulate that they only want to receive the highest possible royalties, if only as a bargaining position to extract as much of the value from an agreement as possible. In Web IV, the Judges found similar "lay testimony" to be "unhelpful and essentially self-serving."[190] This is particularly appropriate given the support *from record labels own strategic documents* (summarized in the next subsection) for the conclusion that non-interactive services enhance download and interactive subscription sales and usage.

(233) Despite their appreciation of this evidence, Dr. Ford is correct that the Judges did not adjust the webcasting rates because (1) they concluded that they had a useful benchmark and (2) any promotional or substitutional effects were necessarily "baked in" to that benchmark. But that does not mean that they didn't find a lack of evidence.

(234) Furthermore, matters are different in this proceeding. As stated in my direct report, in my opinion the PSS musical works market is the best possible benchmark for the PSS sound recording performance market.[191] If the Judges were to adopt this benchmark, they would perhaps conclude, as they did in Web IV, that it already incorporated promotional effects. If, however, the Judges conclude that the PSS musical works rate is an inappropriate benchmark, then, as discussed in my direct report, I conclude that there is no appropriate benchmark for the hypothetical PSS market. As discussed in great detail in Sections II above, it is certainly not the case that the CABSAT market represents a usable benchmark.

(235) In the absence of a usable benchmark, other methods must be used and, in these other methods, an evaluation of promotional effects *could* be appropriate. The evidence presented by Mr. Rosin in Web IV certainly supports the view that interactive and non-interactive services are not close substitutes. In the next sections, I present industry data, strategic documents, and a model of music discovery and consumption that suggest that they could indeed well be complements, and similarly PSS services and other sources of music industry revenue.

V.A.3. Industry data, strategic documents, and a model of music discovery and consumption all support the complementarity of interactive and non-interactive services

V.A.3.a. Overview

(236) When evaluating a technical issue like the nature of substitutability and/or complementarity between services, the Copyright Royalty Judges prefer "detailed financial and economic data" to support their

[190] Web IV at 26327.

[191] Crawford WDT, ¶55-62.

decision-making.[192] Best are scientific studies designed to specifically address this question, produced either by the parties in the proceeding or by independent academics.

(237) Unfortunately, I do not have any such a study to present and academic studies on the substitutability of music services with other sources of industry revenue are unfortunately indeterminate, often identifying the impact of the use of competing services on the consumption of individual songs and not service-level demand as a whole.[193]

(238) In the absence of credible empirical studies, one has to make do with the data available. In the balance of this section, I present aggregate patterns of household service use, industry strategic documents, and a model of music discovery and consumption that suggest non-interactive services like those provided in PSS markets are complementary with record labels' primary sources of industry revenue (digital downloads and interactive services). I also show that it takes only a *very small* promotional effect to have a material effect on the royalty that would arise in the hypothetical market for PSS sound recording performance rights. My goal is this: *if* the Judges decide to there is a case for adjustments to a PSS rate due to promotional or substitutional effects, they should conclude that there *is* a promotional effect of PSS services and that this effect would *lower* a PSS rate from that which I estimate would arise when considering the PSS market on its own (as presented in my direct testimony).

V.A.3.b. Many households subscribe to and use multiple services, especially interactive and non-interactive services

(239) If music services were strong substitutes, then one would generally not see consumers simultaneously using more than one, yet consumer use of multiple platforms is widespread. Figure 1 below reports that, in a July 2016 Ipsos survey commissioned by Music Choice, many Music Choice viewers use

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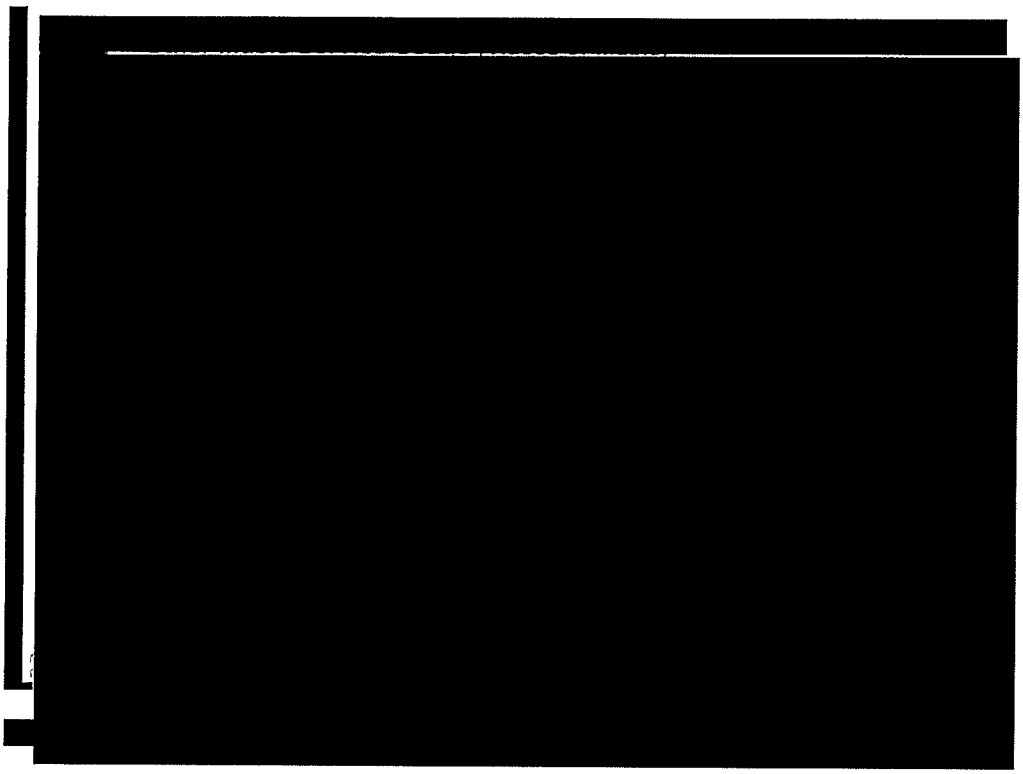
[192] Web IV, 26329.

[193] Hiller and Kim (2014) analyze the impact of YouTube on album sales and finds substitution, with the unavailability of Warner Music songs leading to an increase in sales of best-selling albums (R. Scott Hiller and Jin-Hyuk Kim, "Online Music, Sales Displacement, and Internet Search: Evidence from YouTube," Center for the Analysis of Property Rights and Innovation (CAPRI), Publication 13-2. https://www key4biz.it/files/000263/00026398.pdf). Kretschmer and Peukert (2014) find that YouTube availability (free sampling) has a positive effect on album sales with no effect on sales of digital songs (on iTunes), i.e., the promotional effect of YouTube videos outweighs the displacement effect with no effect on digital sales of songs (Tobias Kretschmer & Christian Peukert, "Video Killed the Radio Star? Online Music Videos and Digital Music Sales," CEP Discussion Paper No. 1265, (April 2014). Centre for Economic Performance, London School of Economics and Political Science). McBride (2014), reporting on Pandora experiments, found that "spinning on Pandora increases music sales by +2.31% for music new to Pandora, and increases music sales by +2.66% for catalog music on Pandora." Similarly, "Pandora increases music sales for new music from major labels by a statistically significant +2.82%" and by +2.36% for catalog music from the major labels (Stephan McBride, (2014): Written Direct Testimony of Stephan McBride (On behalf of Pandora Media, Inc.), http://www.loc.gov/crb/rate/14-CRB-0001-WR/statements/Pandora/13_Written_Direct_Testimony_of_Stephan_McBride_with_Figures_and_Tables_and_Appendices_PUBLIC_pdf.pdf). Aguiar and Waldfogel (2015) find that "interactive streaming appears to be revenue-neutral for the recorded music industry." (Luis Aguiar and Joel Waldfogel, "Streaming Reaches Flood Stage: Does Spotify Stimulate or depress Music Sales?" Institute for Prospective Technological Studies Digital Economy Working Paper 2015/05.)

many other music services. The same survey reported that [redacted] of Music Choice viewers used online sources to listen to music.

Figure 1: Music Choice viewers – other music services usage (videos or music)



(240) Further evidence comes from third-party, service provider, and record-industry surveys. In a Pandora earnings call, Pandora CEO Mike Herring said "Many third parties have shown significant overlap of Spotify, for example's customer base and Pandora's, meaning it's north of 60%, 70% of Spotify users also use Pandora…"[194] Mr. Rosin, in his survey for Pandora in Web IV, found similarly that "[t]he majority (59%) of subscribers to on-demand services also use non-interactive services," concluding "[u]se of both types of services demonstrates that such services are not substitutes, but serve different roles for consumers."[195]

[194] He goes on to say that such overlap leads to promotional effects: "We have lots of anecdotes that show that listening to Pandora introduces listeners to music, new music, that they either purchase and download or add to a playlist when they look to have a lean-in experience, and they would definitely be doing that through one of the on-demand services. So we haven't been able to, because of technical issues, demonstrate that through economic analysis like we have where we can access actual purchase data in terms of albums and downloads, but there's a strong belief that we'll see a similar effect." (Pandora, "Pandora Media Inc. Conference Call to Discuss Web IV Proceeding," earnings transcript. Nov. 18, 2014, 13.)

[195] Rosin WDT, 13.

(241) Similar results come from information solicited by record labels. The 2015 annual music study of MusicWatch to the Recording Industry Association of America (RIAA) reported that [redacted]"[196]

(242) Consumer use of multiple services also isn't simply the case of their trying out a few services before settling down to only use one: MusicWatch's RIAA report also found that [redacted] (emphasis added)]].[197]

(243) Multiple service use, particularly of non-interactive services like Music Choice and interactive services like Spotify, is very hard to reconcile with substitutability but is perfectly consistent with complementarity. Just as few households have both Coke and Pepsi (strong substitutes) in the house, they often have peanut butter and jelly (strong complements). So too for interactive and non-interactive music services.

V.A.3.a. Both industry behavior and internal strategic documents support the view that non-interactive services like Music Choice are complementary with major sources of record label revenue

(244) While Dr. Ford relies on testimony from industry executives Aaron Harrison, Senior Vice President, Business & Legal Affairs, UMG Recordings, Inc., and Michael Kushner, Executive Vice President, Business & Legal Affairs, Atlantic Recording Corporation, to argue that substitution across platforms paying different royalties is "the dominant consideration in the modern music marketplace."[198] *But both industry behavior and strategic documents produced by record labels themselves belie this claim.*

(245) Consider first how the industry treats Music Choice itself. Dr. Ford argues at length that non-interactive services like Music Choice are substitutes for other sources of industry revenue (e.g. downloads, interactive subscriptions).[199] If this were true, *why would the industry work so assiduously to promote their artists to Music Choice?* Promotion costs record labels money, both in staff time and in promotional materials. Why would they spend *any* money if they didn't think there was *some* net benefit? As discussed in my direct report, the *total* revenues record labels earn from the PSS market is on the order of [redacted] million per year, and the impact that promotion of the artists

[196] MusicWatch Inc., "Annual Music Study 2015," Final Report to RIAA Research Committee. Mar. 2016, 55. SoundX_000106537-643.

[197] MusicWatch, Inc., "Annual Music Study 2015," Final Report to RIAA Research Committee, Mar. 2016, 55. SoundX_000106537-643.

[198] Ford WDT, 10.

[199] Ford WDT, 22-23.

within their catalog could earn from the PSS market is therefore tiny.[200] They cannot therefore reasonably expend such efforts due to incremental revenues from the PSS market.

(246) There simply must be *some* incremental benefit to rationalize these promotion expenditures. *The only way such expenditures can be rationalized is if, consistent with the long-held view of Music Choice, there are benefits in terms of promotion of other sources of record label revenue.* This additional promotional effect could only be due to increased sales of CDs or digital downloads, increased plays on subscription webcasting services, or increased plays that increase the ranking of an artist/song (itself leading to increased CD or download sales and/or increased streaming plays).

(247) Experts for SoundExchange sometimes speak of promotion as a "zero-sum" game, but this is wrong in two dimensions.[201] First, promotion of the artists within one label's catalog increases consumer engagement with those artists and with music in general. While some listening to those artists may come at the expense of listening to the artists of other labels, some surely also comes at the expense of time spent not listening to music.[202] Second, I believe that the promotion of the artists belonging to a label's catalog operates in a manner analogous to steering. The "promotional market" is arguably workably competitive – there are no regulations that limit label behavior and there is every indication that labels compete vigorously to enhance the number of plays from artists within their catalog on services generally, including Music Choice.

(248) Why then do they promote them so vigorously? It imposes a cost, so there must be some benefit. I think that it is evident that in the absence of such promotion by a given record label, promotion by rival record labels would enhance the number of plays that those other labels would earn at the given label's expense. This is just the competitive process at work in a dimension other than royalties. Furthermore, even if there were no *net* benefit of the promotional activity relative to a "natural" rate of play for each label's catalog, labels *must* expend such efforts lest they fall behind. And, per the above, the only reason they could rationally do so on a service like Music Choice is due to the promotional effect such expenditures have on other sources of record label revenues. In a nutshell, if plays on Music Choice didn't matter to their other sources of revenue, then they just wouldn't bother with Music Choice.

(249) Consider next industry strategic documents. They demonstrate that the recording industry *itself* understands that the promotion of non-interactive services provides benefits from other sources of revenue. I present two examples of such an understanding.

(250) A first piece of evidence is the recording industry's support for free, i.e. advertising-supported, Internet radio. By their own admission, [redacted]

[200] Crawford WDT, ¶26.

[201] *See,* e.g., Kushner WDT, ¶22.

[202] Indeed, this is one of the findings of Mr. Rosin's survey results summarized in the previous subsection.

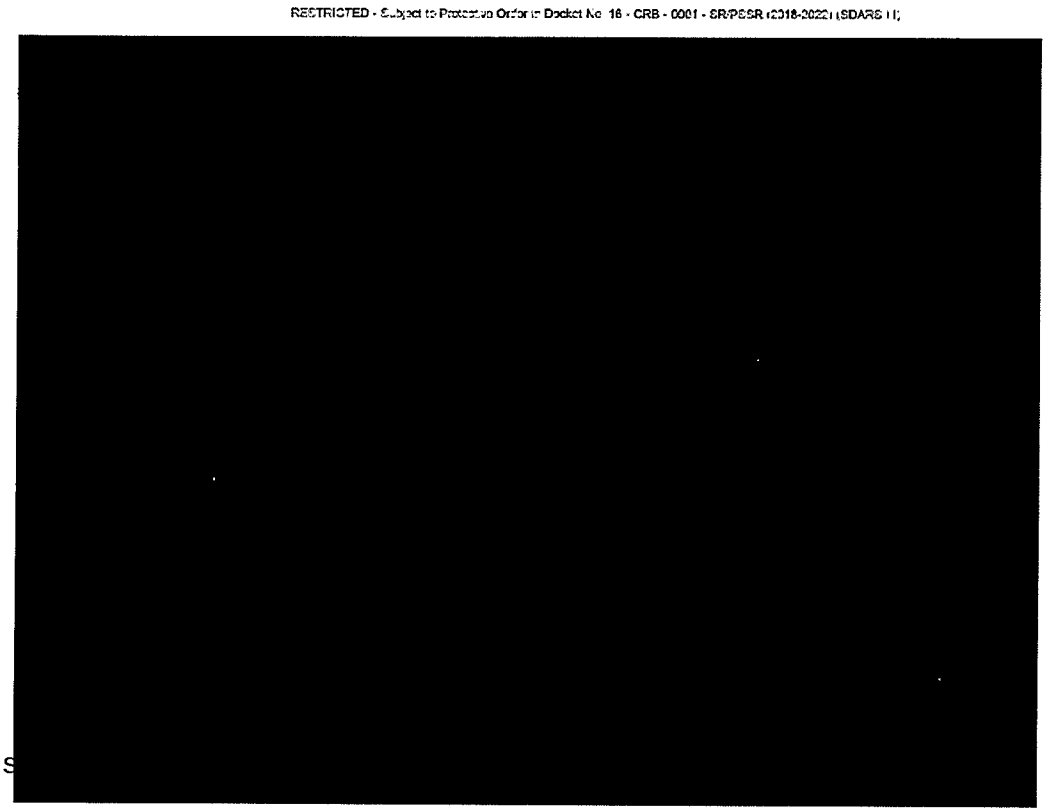
[redacted]

(251) A second piece of evidence is even more direct. Figure 2 below, presents a page from a presentation by Warner Music Group (WMG) describing their corporate digital strategy, including [redacted]

[redacted]

[203] Warner Music Group, "Digital Strategy," Nov. 15, 2012, SX Ex. 011 (SoundX_000076302-330), 19.

Figure 2: Warner Music Group: Digital Radio: Key Strategic Goals and Priorities



(253) The company's view was confirmed only this month, when WMG Executive Vice President Eric Levin, discussing YouTube, said, "Look, YouTube has clearly been a very popular for years consumer opportunity, and there are multiple things where YouTube provides … benefits to promote music…"[204]

V.A.3.b. A modeling approach to predict substitution or promotion

(254) If aggregate data patterns and/or industry strategic documents aren't convincing enough for the presence of a promotional effect of non-interactive services, a final alternative is to model the nature of consumer decision-making in music markets and draw inferences about likely patterns of substitution or promotion from that model. This is a common exercise underlying the estimation of demand for products in any industry or market.

[204] Musically, "WMG says current music-streaming growth is 'just a drop in the bucket," Feb. 8, 2017. http://musically.com/2017/02/08/wmg-says-current-music-streaming-growth-is-just-a-drop-in-the-bucket/. The article further noted that Mr. Levin went "off-message (from an industry perspective)" with this comment, further concluding that "the popularity of YouTube is NOT hampering the growth of subscription audio-streaming services." (emphasis in original).

(255) The literature on demand estimation in economics has identified two important elements driving choices in product markets generally: constructing choice sets and making a choice. In many product markets, choice sets are simple and well-defined: if a consumer wants to buy a pay-television package, they understand that there are a handful of well-known companies offering such services from which they can choose. Given their preferences over the contents of each provider's offered pay-television bundles, they then choose one (or none).

(256) Music markets are more complicated, however. Music is what economists call an "experience good", a product whose characteristics are only learned upon consumption or use. For example, it is hard to know if you will like a song before you've heard it. The same is true for a movie. Unlike many experience goods, however, once identified, music is consumed *repeatedly*: most people only want to see a movie once, but will listen to their favorite music over and over again.

(257) Economists analyze markets with experience goods using models of *search*. In a first stage, consumers decide where and how to search and, in a second stage, they buy and consume the product.[205] In music markets, these stages are well-defined: the first stage describes consumers' process of "music discovery" and the second stage describes the process of (possibly repeated) "music consumption."[206]

(258) The presence of two different processes (serving two different needs) facing consumers in order to satisfy their demand for music has important implications for understanding music markets in general, and the likely nature of complementarity and/or substitutability between services. First, it is possible that different consumers weight differently the importance of music discovery and music consumption, or that the same consumer weights them differently at different points in time. Two needs for consumers, in turn, implies demand for two different kinds of services to satisfy those needs. I think it plausible that a range of non-interactive ("lean-back") service options (e.g., broadcast radio, non-interactive webcasting, and cable radio like that offered by PSS providers) best satisfy the need for music discovery and a range of ownership and interactive ("lean-in") service options (e.g. CD sales, digital downloads, and interactive services) best satisfy the need for music consumption (for that music already discovered to be preferred).

(259) Second, two needs for consumers implies that services that serve each need are likely to try to develop features that best serve that need, even if it makes the service *less* attractive for serving other needs (at least early in each company's development). Thus, non-interactive services are likely to concentrate their energy on providing consumers with music that they both (a) like and (b) might not

[205] *See* George J. Stigler, The Economics of Information, The Journal of Political Economy, Volume 69, Issue 3 (Jun., 1961), 213-225. http://home.uchicago.edu/~vlima/courses/econ200/spring01/stigler.pdf and Jean Tirole, The Theory of Industrial Organization, (Cambridge, Mass: MIT Press, 1988), 106.

[206] *See* Charoenpanich and Aaltonin (2015) for a formal model of music discovery and music consumption. Charoenpanich, Akarapat and Aaltonen, Aleksi, "(How) Does Data-based Music Discovery Work?" (2015). ECIS 2015 Completed Research Papers. Paper 26. http://aisel.aisnet.org/ecis2015_cr/26.

otherwise be exposed to, for example by hiring expert programmers with knowledge and taste, while interactive services are likely to concentrate their energy on providing an intuitive interface that makes it easy for consumers to find specific songs *that they already know they like* and play that music when and where they like.

(260) Of course, many services are beginning to offer features that reflect the needs and desires of other services. Thus Spotify now provides a "radio" or playlist feature to offer consumers a lean-back experience while Pandora has announced that it will release an on-demand music streaming service in 2017.[207] There are two important implications of this fact. First, the fact that services focusing on one of the two needs have determined that it is beneficial to offer features that serve the other need validates the presence of two needs in this market. If interactive and non-interactive services were already indeed close substitutes, why would one need to copy the features of the other type of service? Second, the presence of features seeking to address a service's "non-primary" need (i.e. radio / playlists for Spotify; on-demand for Pandora) does not mean that consumers value highly these non-primary features on those particular platforms. It certainly does not mean that they value these features as highly as the same features offered by services for which those are "primary" needs. In other words, Spotify's radio playlists are not likely to be nearly as good as Pandora's.[208]

(261) Third, two needs for consumers also implies that services serving different needs are more likely to be complements while services that serve similar needs are more likely to be substitutes. The common use of multiple services, particularly mixing interactive and a non-interactive services, described in the previous sub-section bears this out. It is also a specific implication of a general finding within the estimation of demand that products that have similar characteristics are more likely to be substitutes than products that have different characteristics.[209] Thus, two non-interactive services that both provide a lean-back experience, but differ in the quality of their music programming, are more likely to be perceived as substitutes while a non-interactive service and an interactive service that have

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[207] On December 6, 2016, Pandora revealed its $10-a-month on-demand music streaming service, Pandora Premium, stated for release in 2017. *See* Micah Singleton, "Pandora Premium unveiled, coming early next year for $10 per month," The Verse, December 6, 2016. http://www.theverge.com/2016/12/6/13846936/pandora-premium-music-streaming-service. *See also* Pandora Blog, "Coming Soon: Pandora Premium, December 7, 2016. http://blog.pandora.com/us/coming-soon-pandora-premium/.

[208] *See* Glenn Peoples, "Business Matters: Spotify Does Many Things Well, But Radio Isn't One of Them," Billboard, June 12, 2012. http://www.billboard.com/biz/articles/news/radio/1093108/business-matters-spotify-does-many-things-well-but-radio-isnt-one-of ("Spotify has created a fantastic ecosystem for enjoying music, but radio is what it does least well. … Spotify says its radio stations picks songs based on its social graph, or the connections between people, songs and playlists. Competitors take a different approach. Pandora, for instance, chooses songs based on musical characteristics and user feedback. Based on my use of Spotify's radio functions as well as competing products by Pandora, iHeartRadio and Slacker, I think it's safe to say Spotify has the worst radio product of the group.")

[209] *See* Steven Berry, James Levinsohn, and Ariel Pakes, "Automobile Prices in Market Equilibrium," Econometrica, Vol. 63, No. 4. (Jul., 1995), 841-890.

different characteristics designed to serve different needs are more likely to be perceived by consumers as complements.[210]

(262) There is support for the identification of non-interactive services like Music Choice with the music discovery process and interactive services with the consumption process. On the first point, in an July 2015 Ipsos survey commissioned by Music Choice that I cited in my direct report, [redacted] of Music Choice Music Channel viewers reported to be interested in "being exposed to new artists and music."[211] Furthermore, Edison Research in both 2014 and 2016 found that the most important sources for music discovery among music services were non-interactive services like broadcast radio, Pandora, and music television channels (including Music Choice). By contrast, iTunes (a site largely used for digital downloads) and Spotify (an interactive service) were 8th and 9th in reported importance.[212] On the second point, with the growth in interactive service revenues, industry participants are now emphasizing strategies for their music to be *put onto interactive service playlists* to foster repeat consumption.[213]

(263) While not as convincing as detailed empirical evidence, a "dual needs" model of music discovery (provided by non-interactive services) and music consumption (provided by interactive services) also supports the notion that such services are likely to be complementary.

V.A.4. Even a small net promotional effect would yield benefits to record labels equivalent to the total current PSS royalties.

(264) In my written direct testimony, I showed that it takes only [redacted] Music Choice listeners to download a single track per month for any net promotional benefit to record labels from the Music Choice service to be equal to the total royalties record labels currently earn from Music Choice.[214] In Dr. Ford's written direct testimony, he reports estimates from Mr. Aaron Harrison's testimony of the annual benefit to record labels of alternative sources of record

[210] Furthermore, this is likely to be true *even if* each service has some features commonly associated with serving the other need (e.g. an interactive webcaster offering channels or playlists or a non-interactive webcaster offering some portability). The strength of substitution and/or complementarity is a matter of degree, not a matter of kind.

[211] Exhibit MC 15, Ipsos OTX MediaCT, Music Choice Viewership Study July 2015, 27.

[212] Edison Research, "The Infinite Dial 2016," annual study, 2016, 34.

[213] [redacted] (Warner Music Group, "Streaming Overview," Global Digital Summit, Jan. 2015, 7, 11 and 16. SoundX_000040364-380.) Relatedly, Mr. Kushner in his testimony noted that WMG takes part in promotions in various music services to "get crucial positioning on playlists and thus greater market share." (Kushner WDT, 11)

[214] Crawford WDT, ¶217.

label income (CD sales, digital downloads, premium interactive service, etc.). Based on this information, I can update the analysis in my direct report to rebut Dr. Ford's claims.

(265) As I noted there, in 2016, Music Choice is estimated to pay royalties to SoundExchange in the amount of [redacted] When spread over its [redacted] monthly listeners, this amounts to a payment of [redacted] cents per listener per year. If, as described in Mr. Harrison's testimony, record labels earn [redacted] in royalties for those consumers who regularly purchase digital downloads and if a Music Choice listener who purchases digital downloads is like the average digital download purchaser, then it only takes [redacted] Music Choice listeners to become a regular purchaser of digital downloads in order for any net promotional benefit to record labels from its service to be equal to the total royalties record labels currently earn from Music Choice.[215] Using Dr. Ford's numbers, it takes even *fewer* regular music downloaders to provide SoundExchange with Music Choice's total sound recording royalty payments.

(266) While that analysis focused on digital downloads, in Dr. Ford's written direct testimony, he emphasizes the importance instead of interactive subscriptions on the music industry's long-run profitability.[216] My conclusion above is just as strong if not stronger, however, when considering the streaming market.

(267) In order to perform a calculation similar to that above for digital downloads, it is useful to have an important data point: the average number of streams per song on an average on-demand streaming service. After considerable research efforts, I have concluded there does not appear to be an industry-wide consensus on what is the average number of streams per song.

(268) As such, I use the two best estimates of this information I was able to find. First, a website seeking to help rightsholders understand how such interactive services function reported that the average number of streams per song in 2016 for an "indie" label with approximately 150 albums in its catalog and 115 million streams concluded that the average stream per song was 154.[217] Second, there *is* consensus on the ratio of streams to a single download to an album sale that the industry uses to construct measures of top album sales: all of the RIAA, Nielsen, and Billboard agree that 150 on-demand streams equates to one (1) digital download.[218] The RIAA, in its press release in February 2016 reporting this

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215 [redacted]

216 Ford WDT, 12. ("Now, both CD and download sales are falling as the revenue from digital streaming/satellite services are rising.")

217 The Tricordist, "Updated! Streaming Price Bible w/ 2016 Rates: Spotify, Apple Music, YouTube, Tidal, Amazon, Pandora, Etc." Jan. 16, 2017. https://thetrichordist.com/2017/01/16/updated-streaming-price-bible-w-2016-rates-spotify-apple-music-youtube-tidal-amazon-pandora-etc/. (Accessed Feb. 13, 2017).

218 RIAA, "RIAA Debuts Album Award With Streams," Feb. 1, 2016. https://www.riaa.com/riaa-debuts-album-award-streams/, accessed February 6, 2017; Billboard, "Billboard 200 Makeover Album Chart to Incorporate Streams & Track Sales," Nov. 19, 2014. http://www.billboard.com/articles/columns/chart-beat/6320099/billboard-200-makeover-streams-digital-tracks; Christopher Morris, "Nielsen SoundScan to Integrate Streams, Downloads into Album Sales Chart", Variety, Nov. 19, 2014. http://variety.com/2014/music/news/nielsen-soundscan-to-integrate-streams-downloads-into-

ratio, said it was set "[a]fter a comprehensive analysis of a variety of factors – including streaming and download consumption patterns and … consultation with a myriad of industry colleagues."[219] In what follows, I assume that the average song streamed on an online service is streamed 154 times; using 150 instead would yield qualitatively similar results and any adjustments in this value would only serve to scale the conclusions I draw below by the associated scale factor.[220]

(269) Based on this assumption, I can calculate what share of Music Choice subscribers must stream a song this average number of times after hearing it on Music Choice in order to provide SoundExchange with revenue equal to the total of their (Music Choice's) PSS royalties. To do so, I note that Spotify, the largest interactive service, reports that it pays between $0.006 and $0.0084 per stream to rightsholders and Royalty Exchange (a marketplace to conduct royalty auctions) estimated that 85.7% of those payouts went to record labels for sound recording performance rights.[221] Using the lower end of Spotify's per-stream payout to be conservative, a lower bound on Spotify's payout to record labels per year is $0.0051 per stream, or $0.792 (79.2 cents) per year for the average song (154). Comparing this with the [redacted] cents per listener per year SoundExchange earns from Music Choice, it only takes roughly [redacted] Music Choice listeners to stream *a single song* for an average number of times in a year because they heard it on Music Choice for SoundExchange to recoup the entire revenues it earns in that year in sound recording performance royalties from Music Choice.

(270) Following the same line of analysis I take in my written direct testimony, if the current (regulated) royalty rate were the outcome that would arise in a hypothetical market with equal bargaining power and no promotional effect, a promotional benefit of roughly [redacted] Music Choice subscribers to stream a single song for an average number of times because they heard it on Music Choice would be sufficient to establish a *zero* royalty in the PSS market.[222]

(271) Note that these result are for an average Music Choice subscriber streaming a single song an average number of times. As summarized in the last subsection, given that many Music Choice subscribers use Music Choice to learn about music and are therefore likely to stream many more than one song, it

album-sales-chart-1201360668/.

[219] RIAA, "RIAA Debuts Album Award With Streams," Feb. 1, 2016. https://www.riaa.com/riaa-debuts-album-award-streams/, accessed February 6, 2017.

[220] A crude back-of-the-envelope calculation suggests 150 streams for the average song isn't likely to be far off the mark.

[221] Spotify, "How is Spotify contributing to the music business? https://web.archive.org/web/20160108145231/http://www.spotifyartists.com/spotify-explained, Royalty Exchange, Music Royalties Guide, https://www.royaltyexchange.com/learn/music-royalties#sthash.V2gW2plM.fuAnj9SI.dpbs, both accessed February 6, 2017.

[222] As I show in paragraphs 217-218 in my written testimony, if the current (regulated) royalty rate were the outcome that would arise in a hypothetical market with equal bargaining power and no promotional effect, a promotional benefit of twice the size of current PSS revenues would be enough to make the joint surplus in the PSS market zero, establishing a zero royalty. As such, one needs twice as many Music Choice subscribers [redacted] to stream the average number of songs in a year to achieve this outcome.

makes it even more likely that, if there is a significant promotional effect of the Music Choice service, the value of this promotional effect far outweighs the value to SoundExchange of PSS royalties. For example, if a devoted Music Choice listener streamed 20 songs per year for the average (154) number of streams because she heard them on Music Choice, it would only take [redacted] Music Choice's subscribers to be such a devotee (along with *no* streaming for any other Music Choice listeners) for the revenues to SoundExchange from that streaming in that year to equal the total of Music Choice's PSS royalties in that year.[223]

(272) I can get at the same effect without relying on an uncertain value for the average number of streams per song using a slightly different calculation. For the period December, 2015-May, 2016, the average Spotify user played [redacted] streams per month and an average Apple Music played [redacted] streams per month.[224] Averaging these numbers (to roughly [redacted] streams per month), this yields roughly [redacted] streams for an average Spotify or Apple Music user per year. Given the calculations above, record labels receive approximately the same revenue from a Music Choice subscriber [redacted] as someone who plays approximately [redacted] streams per year [redacted]). From the calculations above, [redacted] streams is *under* [redacted] *of the number of streams of an average Spotify or Apple Music user.*

(273) Given that Figure 1 above showed that [redacted] of Music Choice listeners have ever used Spotify and, of these, [redacted] (or [redacted] of all Music Choice listeners) use it daily or almost daily, I find it quite likely that there are promotional benefits to record labels of Music Choice.[225] For example, if these [redacted] of Music Choice listeners are like the average Spotify or Apple Music user, they need only stream [redacted] songs per year, or [redacted] of their average streaming for the year, due to music they heard on Music Choice, for the total revenue from their behavior to equal that which Music Choice pays to SoundExchange for that year.[226]

(274) I find it very likely that some Music Choice listeners hear new music, add it to playlists on their preferred interactive webcasting service, and stream it regularly over the next year. I therefore find it very likely that *the promotional benefits of Music Choice's services are consequential to record label revenues*. Or, at minimum, more consequential to their revenues than Music Choice's PSS revenues! Furthermore, since most users stream songs for far longer than a year, even this calculation is conservative, as the profits from such streaming will continue far past the single year's PSS royalties.

(275) Given the relatively small benefit to record labels of PSS royalty payments, almost *any* promotional effect would have a significant impact on bargaining outcomes in the hypothetical market for PSS

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223 [redacted] and [redacted]

224 Universal Music Group, All-Partner Business Review, July 2015. SoundX_00000045662-690, at 25.

225 This illustration using only daily users is conservative because it does not include intermediate and low-frequency users that are factored in the overall industry average.

226 [redacted] and [redacted]

sound recording performance rights, and suggests sound recording performance royalties for the 2018–2022 period would be lower even than that predicted by the rate of 3.5% of residential service revenues (and no higher than 5.6%) that I concluded in my direct report would arise in the hypothetical PSS market.

VI. Conclusion

(276) In this rebuttal report, I evaluate the merits of the analysis and the evidence presented in the written direct testimonies of Dr. Paul Wazzan, Mr. Jonathan Orszag (as part of Dr. Wazzan's testimony), and Dr. George Ford submitted to the Copyright Royalty Judges and on behalf of SoundExchange regarding the statutory royalty rate for digital performance rights in sound recording for pre-existing subscription services ("PSS") such as Music Choice.

(277) As discussed at length above, Dr. Wazzan supports using the CABSAT royalty as a benchmark for a PSS sound recording performance royalty. The reasons that I have presented above that the Judges should reject this benchmark are many: CABSAT rates arise from a litigation settlement between the single rightsholder and a single rights user who treats the CABSAT market as promotional; the demand, cost, and competitive conditions of the CABSAT market are different from those in the PSS market and Dr. Wazzan doesn't adjust for these differences; they imply that no firm could offer a PSS service as a stand-alone business, and they do not appropriately account for the 801(b) policy factors. Based on these analyses, I conclude there is simply no justification whatsoever for using the CABSAT rate as a benchmark in this proceeding.

(278) I also show that Dr. Wazzan's conclusions on a number of other topics are also faulty: PSS rates should continue to be set as a percentage-of-revenue, they should absolutely include the right to retransmit PSS programming over the Internet, and the patterns of Music Choice's rates paid by its cable partners are perfectly consistent with patterns of size discounting in the industry. The Judges should therefore also reject each of Dr. Wazzan's counter-arguments on these topics.

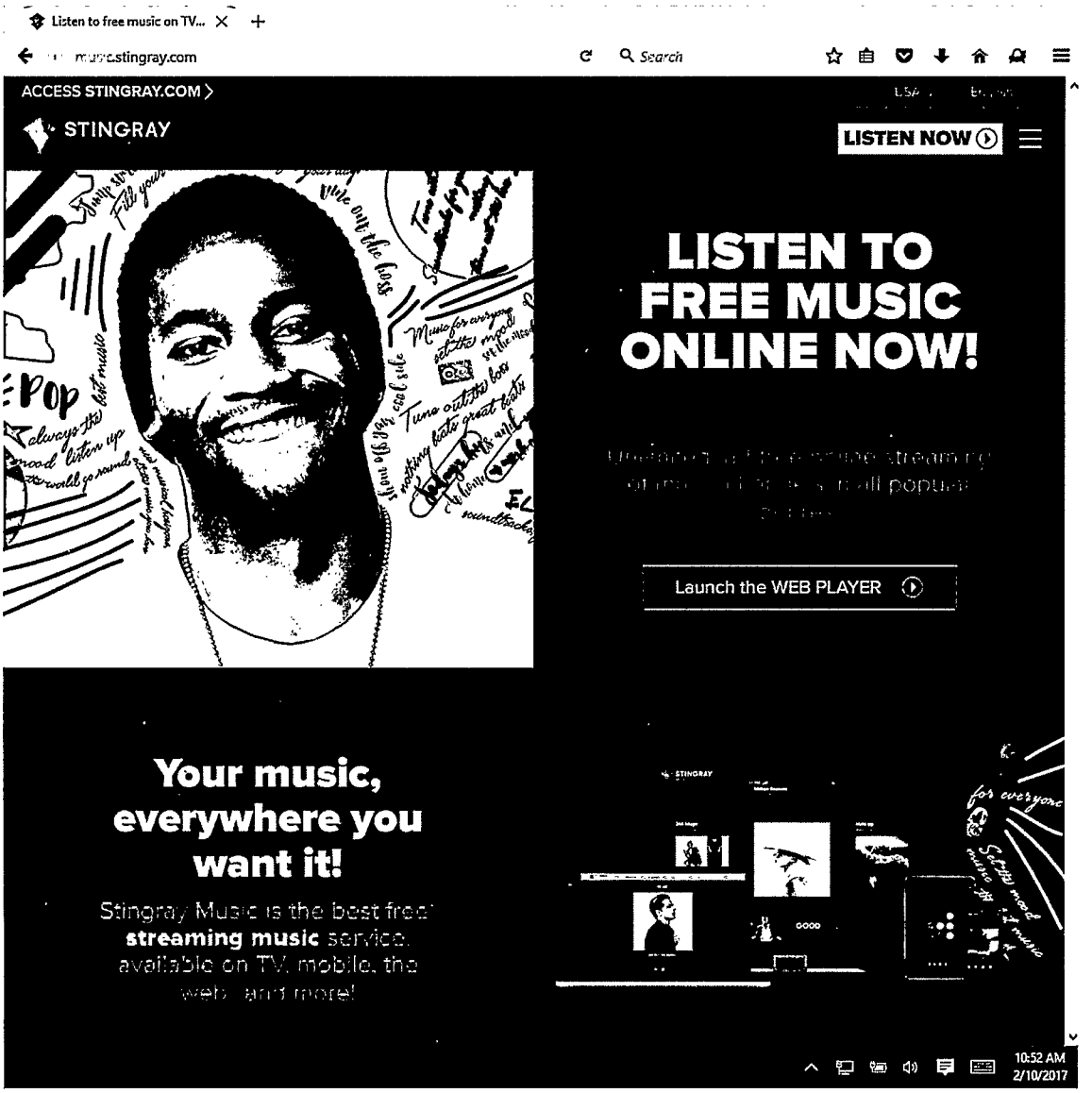
(279) Turning to Dr. Ford, while his analysis seeks to enlighten whether or not non-interactive services like PSS are substitutional or promotional for other sources of recording industry revenue, he simply fails in this task. While this is a difficult question on which to find convincing evidence, I find Dr. Ford's evidence unpersuasive. By contrast, counter-evidence on this question that I present strongly suggests that there *is* a promotional effect of PSS services on other sources of music company revenue. Furthermore, I show that even a small such effect would significantly lower the rate that would arise in a hypothetical market for PSS sound recording performance rates relative to one that ignored such an effect.

(280) Having not been convinced by the evidence presented by Drs. Wazzan and Ford, I continue to recommend to the Judges to rely on the model-based approach I took in my direct testimony and recommend a royalty for PSS sound recording performance rights of 3.5% (and certainly no higher than 5.6%), with possible downward adjustments due to the likely promotional effects of PSS services.

Appendix A. Stingray website and Stingray Music reviews

A.1. Stingray Music US website

Exhibit A.1: Stingray Music US website



Source: http://music.stingray.com/music-online-service/. (accessed Feb. 10, 2017).

A.2. Stingray Music on AT&T U-verse reviews

(281) The following examples highlight the important differences between Music Choice and its replacement Stingray Music available on AT&T U-verse in terms of delivery method, the quality of on-screen information, the availability of music videos, the presence of commercials, the difficulty in navigating interface, and music availability.

(282) The excerpts are from two consumer boards (both accessed Feb. 8, 2017):

- ATT Uverse board of the National Consumer Complaint Forum[227]
- AT&T Community Forums[228]

1. Delivery method
   - "Stingray SUX!... One primary difference is that Stingray *REQUIRES* high speed interent service, so if you dont already have that, then Stingray wont work."[229] (Mar. 3, 2015)
   - "Music Choice is Awesome and now it seems like I can't listen to music on the tv now."[230] (Mar. 2, 2015)
   - "I am another person that can't stand Stingray… When my toddler grandkids are over with Music Choice we could flip to different stations quickly so they could dance to different types of music which you can't do anymore because Stingray has to load... [P]lus isnt Music Choice an American company? Go USA!"[231] (Mar. 5, 2015)
   - "The service is provided in an over the top fashion (much like you access Netflix or other streaming services) which is why its so cumbersome… [L]istening to music in monotone is not what I consider tunes. Can you at least deliver the service in stereo? This is like listening to an AM radio."[232] (Oct. 2, 2015)
   - "With MC I could easily channel surf as with nonmusic channels and instantly hear what song was being played. [Stingray] only lets you access a specific music channel at a time through a portal that is annoyingly slow. Once in, if you want to go to a different music

[227] National Consumer Compliant Board, "Consumer complaints and reviews about ATT Uverse," page 1: https://www.complaintboard.com/att-uverse-l3918 html and page 2: https://www.complaintboard.com/att-uverse-l3918/page/2. (accessed Feb. 8, 2017)

[228] AT&T Community Forums, U-verse TV Forum," Page 1: https://forums.att.com/t5/U-verse-TV-Apps/What-happened-to-Music-Choice/td-p/4199475 and page 2: https://forums.att.com/t5/U-verse-TV-Apps/What-happened-to-Music-Choice/td-p/4199475/page/2. (accessed Feb. 8, 2017)

[229] AT&T Community Forums, 1.

[230] *Ibid.*

[231] *Ibid.*

[232] National Consumer Complaint Forum, 1.

channel, you must Exit Stingray, then choose another music channel and finally reenter through the portal again. There is NO channel surfing ability within the Stingray program… The delay in going through the portal is annoying."[233] (Sep. 7, 2015)

2. Quality of on-screen information [234]
   - "My husband and I are totally disappointed with Stingray Music. We have been with UVerse for a very long time. We loved Music Choice. The choices were great!! We liked the fact that you were given information about the music or songs. You knew the year a song came out and you could identity with certain eras" (Jun. 6, 2016)
   - "Too much of the same old stuff. Limited variety of performing artists. The old music channels were much much better and were very informative with regards to the songs and artists history. Stingray is a complete disappointment." (Oct. 22, 2015)
3. Availability of music videos
   - "Stingray music has less music genres, as well as the songs that they play are old or unknown… Also not all videos are on Stingray music, like with Music Choice."[235] (Jun. 6, 2015)
4. Presence of commercials
   - "Prior to Stingray you could just turn on the channel and listen to music... Now Stingray imbeds commercials and keeps stopping"[236] (Apr. 25, 2015)
5. Difficulty navigating interface
   - "[W]hat I've read from other AT&T users is that they're struggling on navigating Stingray stations where Music Choice was easier to navigate."[237] (Mar. 5, 2015)
   - "I still have to say that Music Choice was just plain easier to use."[238] (Mar. 21, 2015)
   - "I have solved my problems with Stingray by not using it at all! Too cumbersome and I don't like the music choices. So now I use the radio on my iPad with a small speaker."[239] (Mar. 27, 2015)
   - "It's also ridiculous to use, it's almost like a music app. It takes you to a whole new page when you have to maneuver from different style of music in the same genres. I like music

[233] *Ibid.*
[234] *Ibid.*
[235] National Consumer Complaint Forum, 2.
[236] *Ibid.*
[237] AT&T Community Forums, 1.
[238] *Ibid.*
[239] AT&T Community Forums, 2.

choice where I could literally put it on channel 11111 amid music would just begin playing. The choice to switch to string Ray was awful and I'm so disappointed."[240] (Dec. 20, 2015)

6. Music availability

- "I listened to the Rock Music Choice channel 5113 which is 'current' rock music – nothing compared to what Stingray considers rock music…Clicking the channel Up/Down button is not even an option. What a complete waste of time."[241] (Mar. 2, 2015)
- "Stingray is terrible. Terrible selection, slow to load, loses connection often. Old channels were fabulous! The Stingray Spa channel is no more spa music than fly to the moon."[242] (Jun. 22, 2015)
- "We have finally quit listening to their channels; their music selections are anything but enjoyable and the channel displays are nothing short of ugly."[243] (Aug. 10, 2015)
- "The music picker on this channel must be 12 or 112...not sure which."[244] (Jul. 7, 2015)
- "Why are 17 of the 75 music channels featuring music that aren't even from my continent?"[245] (Mar. 3, 2015)
- "I really do dislike the Stingray music channels. The selection for the genre is questionable."[246] (Mar. 26, 2015)
- "I often listen to music on my tv when I am cooking, cleaning or have company over but my favorite thing about music choice was their Christmas station (sounds of the season) it was the best and had great variety and artists. Stingy rays music selections for all other music genres and Christmas included are terrible. Songs repeat and the variety of artists are slim or the style music I'm looking for can not be found."[247] (Dec. 20, 2015)

(283) "I switched from Comcast to AT&T just for Stingray because I thought I was getting a better variety of music. Stingray has been horrible! …Music lovers in Grand Rapids, beware of the crap AT&T will deliver and NOT take responsibility for!"[248] (Sep. 18, 2016)

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[240] National Consumer Complaint Forum, 1.

[241] AT&T Community Forums, 1.

[242] *Ibid.*

[243] National Consumer Complaint Forum, 1.

[244] *Ibid.*

[245] AT&T Community Forums, 1.

[246] *Ibid.*

[247] National Consumer Complaint Forum, 1

[248] *Ibid.*

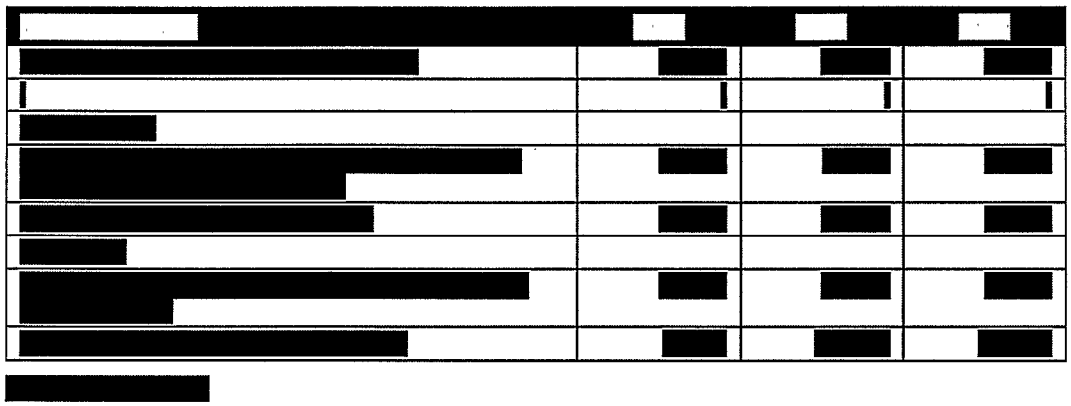
Appendix B. Exhibits

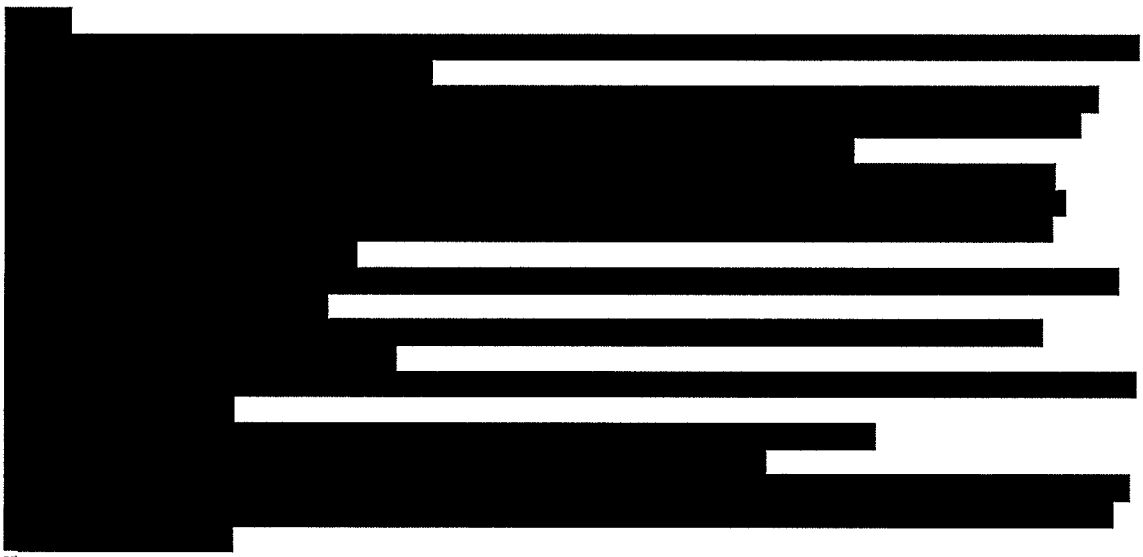
Exhibit B.1: Music Choice Residential marginal costs, non-royalty operating expenses, and capital expenses

[[$ in thousands	2016	2017	2018
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			
[redacted]			

[redacted]

Exhibit B.2: Music Choice's Residential Audio economic Profits at CABSAT royalty rates





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Appendix C. Sound Exchange and RIAA correspondence

- November 29, 2004: Letter from RIAA (Steven M. Marks) to Music Choice (David Del Beccaro, CEO)
- January 10, 2005: Letter from Music Choice (David Del Beccaro, CEO) to Recording Industry Association of America (Steven M. Marks, Esq. General Counsel)
- June 14, 2005: Letter from RIAA (Steven M. Marks) to Music Choice (David Del Beccaro, CEO)
- June 30, 2005: Letter from Music Choice (David Del Beccaro, CEO) to Recording Industry Association of America (Steven M. Marks, Esq. General Counsel)

STEVEN M. MARKS
GENERAL COUNSEL

November 29, 2004

VIA FEDERAL EXPRESS

Mr. David Del Beccaro
President & Chief Executive Officer
Music Choice
110 Gibraltar Road
Suite 200
Horsham, PA 19044

Dear David:

I write to you regarding the launch of two new services by Music Choice, a new broadband offering and My MUSIC CHOICE. As discussed below, these new services are not eligible for the existing 7.25% rate, which is limited to preexisting subscription services of the type offered on July 31, 1998. Further, My MUSIC CHOICE appears to be an interactive service based on our understanding of how it functions, and it therefore requires Music Choice to obtain direct licenses from our members. The purpose of this letter is twofold: (1) to initiate discussions to establish an appropriate rate for Music Choice's new broadband service, and (2) to request that Music Choice promptly seek direct licenses for the new My MUSIC CHOICE service or provide us with information justifying its classification as a non-interactive service.

Music Choice on Broadband

Based on the description in Music Choice's press release of April 5, 2004, Music Choice's new broadband service offers "a content menu with a wide variety of options." Those options include the ability of a consumer to "select exclusive concerts, studio performances, and video interviews." The service also permits a consumer to "download the song or purchase the album." Consumers are also permitted to provide feedback and "identify ten of their favorite channels and store them under "My Channels."

Music Choice's new broadband service thus operates in a different medium than the service offered via cable or satellite television and grandfathered in the Digital Millennium Copyright Act of 1998 ("DMCA"), and includes functionality that takes

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advantage of new capabilities of the broadband medium. This functionality – including the ability of consumers to communicate back with the transmitting entity and receive additional, non-broadcast transmissions – was not available for transmissions via cable or satellite on July 31, 1998.

Both the statute and legislative history make clear that Music Choice's new broadband service does not qualify as a "preexisting subscription service." The statute says that a preexisting subscription service is one that "was in existence and was making such transmissions to the public for a fee on or before July 31, 1998." The legislative history to the DMCA explains that where a preexisting subscription service offers a "new service either in the same or new transmission medium by taking advantage of the capabilities of that medium, such new service *would not qualify as a preexisting subscription service.*" (emphasis added). Rather, the new service would be considered a new type of new subscription service. As such, the rates for the new service – even if made by a company that previously qualified as a preexisting subscription service – would be established under Section 114(f)(2)(B), which provides that the rates to be established are those "that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller," rather than under the Section 801(b) factors.

Because the Music Choice broadband service does not qualify as a preexisting subscription service, it is not eligible for the 7.25% rate established for such services. Instead, Music Choice must pay for the broadband service at some other rate. The rate established for new subscription webcasting could apply or a new rate may have to be established through a separate proceeding. Either way, we would like to speak with you in order to reach agreement that would avoid litigation or arbitration and marketplace uncertainty.

My MUSIC CHOICE

A January 12, 2004 press release describes My MUSIC CHOICE as a service that offers "*custom* music channels for digital cable subscribers." (Emphasis added). The release goes on to state that "My MUSIC CHOICE *enables its viewers to customize music channels* quickly and easily using their television remote to scroll through a few simple television screens that prompt them to choose the types of music by genre, set the mix of selected genres, and enter the name of their custom channel." (Emphasis added).

Based on this description, it would appear that the service makes transmissions that are "specially created" for each listener based on input from that listener. This fact would render My MUSIC CHOICE interactive and ineligible for statutory licensing. We therefore request that you promptly seek direct licenses from our member companies for this service.

If you believe that our view of the My MUSIC CHOICE service is mistaken, we encourage you to provide us with information demonstrating that this service is non-interactive. We note that even if the My MUSIC CHOICE service is non-interactive, it would not be a preexisting subscription service for the same reasons described above in the discussion of the broadband service. The two-way communication between the end user and Music Choice permitting the user to customize the genre mix delivered to such user renders the service a new type of new subscription service requiring a new rate.

Conclusion

Thank you in advance for your prompt attention to the matters raised in this letter. We and our members look forward to speaking with you further about Music Choice's new services, and working with you to bring consumers exciting ways to enjoy digital music.

Very truly yours,

Steven M. Marks

cc: Paula Calhoun
Fernando Laguarda

MUSIC CHOICE®

David J. Del Beccaro
President

110 Gibraltar Road
Suite 200
Horsham, PA 19044
215.784.5840
Fax: 215.784.5870
www.musicchoice.com

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VIA FACSIMILE & REGULAR MAIL

January 10, 2005

Steven M. Marks, Esq.
General Counsel
Recording Industry Association of America
1330 Connecticut Avenue, N.W., Suite 300
Washington, D.C. 20036

Dear Steve:

Thank you for your letter of November 29, 2004. As you know, Music Choice respects the rights of copyright owners and values its good relationship with your organization and its members. We have paid substantial royalties to sound recording copyright owners and complied with applicable reporting requirements and programming restrictions under the Copyright Act since they were first imposed in 1995. We appreciate the opportunity to update you on our program offerings.

The Music Choice residential audio service is a "preexisting subscription service" that performs sound recordings by means of non-interactive, audio-only subscription digital audio transmissions. The same service is transmitted to cable subscribers via satellite, cable headends, and cable infrastructure. Depending on how the signal is coded, it can be received through television set-top boxes or personal computers. The service has the same functionality whether delivered over the television or personal computer (i.e., an individual selects and listens to one channel at a time). The "broadband" description noted in your letter merely refers to the ability of cable listeners to receive the Music Choice audio channels over personal computers on a subscription basis, which has been possible since before July 31, 1998 and is not a change in the preexisting subscription service.

Music Choice does not offer personalized transmissions that are specially created for a particular recipient and are available only to some listeners but not to others. Music Choice does not allow listeners to select particular sound recordings or artists, or to skip, pause or rewind programming. Nothing about "My MUSIC CHOICE" alters or affects this in any way. Rather, it refers to the ability of listeners to select additional Music Choice channels as part of the preexisting subscription service. We do not believe that the provision of additional music channels, programmed in compliance with statutory restrictions (e.g., the "sound recording performance complement") and available to all listeners on the same subscription basis, gives rise to an "interactive service" under the Copyright Act or otherwise disqualifies the service as a preexisting subscription service.

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For these reasons, we are confident that Music Choice's preexisting subscription audio service complies with applicable law and is licensed. We hope that the foregoing information has clarified the issues raised in your letter. Please do not hesitate to contact me again if you have any further questions related to the above.

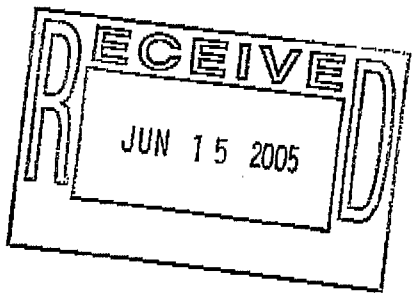
Sincerely,

David Del Beccaro

cc: Paula Calhoun, Esq.
Fernando Laguarda, Esq.

STEVEN M. MARKS
GENERAL COUNSEL

June 14, 2005



VIA FEDERAL EXPRESS

Mr. David Del Beccaro
President & Chief Executive Officer
Music Choice
110 Gibraltar Road
Suite 200
Horsham, PA 19044

Dear David:

I write to follow up on our earlier correspondence concerning two newer services being offered by Music Choice, a broadband service (the "Broadband Service") and My MUSIC CHOICE along with a brand new service, Music Choice for Mobile, that Music Choice is offering to Sprint's mobile phone service subscribers (the "Mobile Service"). (The three services mentioned above are collectively referred to below as the "New Services.") After reviewing your response with our member companies, we were unpersuaded by any of the arguments raised in your letter. As such, we now affirm the initial conclusion set forth in our earlier letter, namely, that none of the New Services qualify as a preexisting subscription service ("PES") and that none of them is eligible for the 7.25% royalty rate.

As explained more fully below, we have determined that the Broadband Service and the Mobile Service are both new subscription services and the My MUSIC CHOICE service is an interactive service, which is outside the statutory license altogether. Accordingly, the Broadband Service and the Mobile Service must immediately start making monthly royalty payments to SoundExchange at the applicable new subscription service rates and must each make lump-sum payments to SoundExchange no later than July 1, 2005 to cover the underpayment of royalties from each service's date of inception through the present. The My MUSIC CHOICE service must immediately remove all sound recordings owned by our member companies from the service unless and until the appropriate licenses are negotiated with our member companies.

The Broadband Service

As you know, the test for determining whether a new service qualifies as a PES is whether the transmissions at issue are similar in character to the transmissions that were being made by the licensee on or before July 31, 1998. Services that take advantage of

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the capabilities of a particular medium, and services that offer video programming (other than information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording) do not qualify for treatment as a PES. See H.R. Conf. Rep. No. 796, 105th Cong., 2d Session at 89 (1998).

The Broadband Service clearly takes advantage of the capabilities of the broadband medium. It does so by, for example, offering users the ability to download or purchase music. It also offers video programming that goes far beyond that permitted under the legislative history (i.e. the videos provide more data than mere information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording.) For both of these reasons, the Broadband Service fails to qualify as a PES.

As such, the Broadband Service must begin calculating and paying monthly royalties to SoundExchange as of June 1, 2005 at the rates established for new subscription services (i.e., the new rate will be reflected in Music Choice's July 20 royalty payment to SoundExchange) and it must make a lump-sum payment to SoundExchange not later than July 1, 2005 to account for the shortfall in payments through May 31, 2005. This lump-sum payment should be equal to the difference between the payments already made by the Broadband Service at the PES rate and the amount the Broadband Service should have paid at the new subscription service rates since the inception of the Broadband Service.

As you may be aware, new subscription services currently have a choice of paying royalties at the rate of $.000762 per performance, $.0117 per aggregate tuning hour (for music intensive programming) or 10.9% of subscription service revenues (with a 27 cents per subscriber per month minimum). For further information about these rates and the applicable definitions, see 37 C.F.R. §§ 262.2, 262.3. These rates took effect as of January 1, 2003 and will remain in effect through December 31, 2005 (or until new rates are set for the 2006-2010 license period).

The Mobile Service

The Mobile Service fails to qualify as a PES for the same reasons as the Broadband Service. Like the Broadband Service, it takes advantage of the capabilities of the wireless medium by, for example, offering users on-demand access to Music Choice content and video programming (i.e., that is not merely information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording.) As such, Music Choice may not pay royalties for the Mobile Service at the rates established for the PES.

Unlike the Broadband Service, the Mobile Service is not covered by the existing rates for new subscription services, as those rates were developed prior to the launch of any wireless music subscription services. However, in light of the fact that wireless services will presumably be covered by the rates established for the 2006-2010 license

period, our members would – for the sake of convenience – be willing to accept payment for the Mobile Service at the existing new subscription service rates for the period from the launch date of the Mobile Service through December 31, 2005.

As such, the Mobile Service must begin calculating and paying monthly royalties to SoundExchange as of June 1, 2005 at the rates established for new subscription services (i.e., the new rate will be reflected in Music Choice's July 20 royalty payment to SoundExchange) and it must make a lump-sum payment to SoundExchange not later than July 1, 2005 to account for the shortfall in payments through May 31, 2005. This lump-sum payment should be equal to the difference between the payments already made by the Mobile Service at the PES rate and the amount the Mobile Service would have paid, had it been paying at the new subscription service rates since its inception.

My MUSIC CHOICE

Based on further discussions with our members, we have concluded that the My MUSIC CHOICE service is interactive and is, therefore, ineligible for the statutory license. The statutory definition of an "interactive service" was amended in 1998 to make clear that "personalized transmissions -- those that are specially created for a particular individual—are to be considered interactive." Conference Report at 87. According to the (amended) statutory definition, an "interactive service" is one that "enables a member of the public to receive a transmission of a program specially created for the recipient, or on request, a transmission of a particular sound recording, whether or not as part of a program, which is selected by or on behalf of the recipient. . . ." 17 U.S.C. § 114(j)(7).

The fact that My MUSIC CHOICE users create personalized channels from preexisting, preprogrammed channels does not change the fact that the relative mix of preexisting channels comprising each user's custom channel is *specially created* by each individual user to suit his/her personal musical tastes. Nor does it matter that users are not permitted to select individual artists or tracks when creating their custom channel. Each user still ends up with a mixture of preprogrammed channels that is specially created by and for them. See Conference Report at 87 ("The recipient of the transmission need not select the particular recordings in the program for it to be considered personalized . . . .").

In light of our conclusion, we expect Music Choice to immediately commence negotiations with our member labels to obtain the licenses necessary to cover the transmissions made by the My MUSIC CHOICE service. Until such licenses are in place, Music Choice must either remove all sound recordings owned or controlled by our member companies from the My MUSIC CHOICE service or cease operating the service altogether.

Thank you in advance for your prompt attention to the matters raised in this letter. Please feel free to contact me if you have any questions about what Music Choice must do to comply with the terms of this letter.

We await your response.

Very truly yours,

Steven M. Marks

cc: Paula Calhoun
Fernando Laguarda

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CONFIDENTIAL
VIA FACSIMILE & REGULAR MAIL

June 30, 2005

Steven M. Marks, Esq.
General Counsel
Recording Industry Association of America
1330 Connecticut Avenue, N.W., Suite 300
Washington, D.C. 20036

Dear Steve:

This letter responds to your letter of June 14, 2005 concerning three services offered by Music Choice. One of these is a broadband residential audio service, another is the same service offered to Sprint's mobile phone service subscribers, and the third is the "My MC" offering. As to the first two, you assert they are not preexisting subscription services and thus are ineligible, in your opinion, for the 7.25% rate established for such services. As to the third, you assert it is an interactive service and as such ineligible for the statutory license. We have carefully reviewed your letter along with our earlier correspondence on this issue, and respectfully disagree.

Here's why. There is no doubt Music Choice is a preexisting service within the meaning of 17 U.S.C. §114(j)(11): the Conference Committee report on the DMCA expressly refers to us. H.R. Rep. No. 796, 105th Cong., 2d Sess. 89 (1998). It is also clear that Music Choice is not limited to the transmission medium in existence on July 31, 1998. The Conference Committee report says that the grandfathered rights extend to "any new services in a new transmission medium where only transmissions similar to the[] existing service are provided."

The report then gives the following, quite apposite example: "if a cable subscription music service making transmissions on July 31, 1998, were to offer the same music service through the Internet, then such Internet service would be considered part of a preexisting subscription service." We deliver the same audio music service as our cable subscription service over a closed network to cable subscribers' computers. If delivering such service over the Internet is considered part of the preexisting subscription service, as the report clearly states, then certainly our audio broadband service should be considered part of the preexisting subscription service.

The key to determining whether a preexisting service offered in a new medium qualifies for the preexisting service rate is *not* the nature of the medium or the fact that a new

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medium is employed (as you apparently assert) but, rather, as the report states, whether the content of the transmission is similar to the one in existence on July 31, 1998. Our broadband service is.

It is true that the committee report refers to "taking advantage of the capabilities" of a new transmission medium, but this language comes after the reference to the Internet – and thus cannot preclude using a new medium – and, moreover, the report then gives an example of what it does mean by this phrase: it gives the example of a service that post-July 31, 1998 begins offering "video programming, such as advertising or other content...."

What the report has in mind is a previously existing audio service that, due to new broadband capabilities, now offers a new type of transmission, that is audio programming mixed with video. But even this is allowed in some circumstances, as the report continues, so long as if the video programming contains information about the service, the sound recordings being transmitted, the artists, composers or songwriters or is an ad to purchase the sound recording.

In taking a contrary view from ours, we believe you misunderstand the nature of our service and Congress's intent. The music transmission as it existed before July 31, 1998 is the same now. We have not added video programming to it. We do offer video programming, but that is on a different transmission and is separately licensed. Although the interface for the broadband Music Choice service allows listeners to switch over to this other, separately licensed, service providing the video transmissions, we do not read the Act to preclude a service such as ours from doing so. Congress only intended to preclude us from including video programming into an existing audio transmission and then relying on the compulsory license for the now mixed transmission. Since audiovisual works aren't subject to compulsory licensing under Section 114, this makes sense: it prevents grandfathered services from distorting the compulsory license. But our music transmission isn't mixed: it is still pure audio, and as such it remains faithful to the compulsory license.

We are somewhat puzzled by your apparent reading of the statute. Under that reading, simply because we have to separately license our new video service at market rates, we must also pay higher rates for the same audio programming service as existed before July 31, 1998. In other words, you appear to be arguing that Music Choice must pay a higher fee for its preexisting audio programming service not because that service has changed materially – it has not – but solely because we now separately license video programming for a different transmission as part of a different service. Congress could not have intended that result. We therefore adhere to our position that we are entitled to the preexisting rate for the audio programming service.

This analysis applies equally to our wireless service. As with the broadband service, the wireless interface may allow users to also access other, separately licensed services, but the underlying Music Choice audio transmission service provides the same channels and

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programming as the original and broadband services. As long as the content transmitted by the wireless service is similar to the content provided by our preexisting service (and it is), Music Choice is entitled to rely on the preexisting rate.

The final issue is whether My MC is interactive. We believe you misunderstand the My MC portion of our audio service. As an initial matter, though, we are very surprised RIAA is concerned with our genre-based channels. In the LAUNCHcast litigation, the LAUNCHcast service offered genre channels, but those channels were not the basis of the suit and we understand RIAA may have taken the position that such stations do not make a service interactive. That makes perfect sense. Congress's concern with interactivity, found in the initial 1995 definition, was with displacement of sales: if a consumer could so influence what he or she heard that there was no need to buy a sound recording, the record company lost a sale. That is not true for genre stations, which instead boost consumer awareness of performers and therefore increase sales.

In any event, nothing in the 1998 amendment to the definition of "interactive service" changes the result for our service. While we recognize that a certain reading of our marketing materials, without an understanding of how the service actually works, might have given you the wrong impression, it is simply not true that there is a custom channel for any user. All users who select the same mix of genres hear the same music at the same time. Music Choice has created a pre-programmed channel for every permutation of possible mixes of genres. When a user selects a particular mix of genres, that user is served an audio transmission that Music Choice, not the user, has selected. Where more than one user selects the same mix of genres, all such users will receive the same transmission and at the same time. Contrary to your letter, no user "ends up with a mixture of preprogrammed channels that is specifically created by and for them."

In light of the further explanation, above, of how our services actually function, we re-iterate our position that the audio programming services we offer via broadband and wireless media fall within the statutory license for pre-existing services because they offer the same programming as Music Choice's cable service. The My MC portion of our service is non-interactive because no program is ever specially created for an individual user. Instead, all users who select the same blend of genres hear the same program at the same time. We trust this resolves the matter and that the labels will be pleased that we are continuing to provide them with exposure for their artists.

Sincerely,

David Del Beccaro

cc: Paula Calhoun, Esq.

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Appendix D. CABSAT Settlement Agreement and Negotiation documents

D.1. CABSAT Settlement Agreement

- SoundX_000477524-836. CABSAT Settlement Agreement, Dec. 11, 2014.

CONFIDENTIAL FOR SETTLEMENT PURPOSES

Execution Copy

CABSAT Settlement Agreement

This CABSAT Settlement Agreement ("Agreement"), dated as of December 11, 2014 (the "Execution Date"), is made by and between SoundExchange, Inc. ("SoundExchange") and Sirius XM Radio Inc. together with its subsidiaries (collectively "Sirius XM"). SoundExchange and Sirius XM are each referred to as a "Party" and collectively as the "Parties."

WHEREAS, the Copyright Royalty Judges ("CRJs") published in the Federal Register at 79 Fed. Reg. 410 (Jan. 3, 2014) a notice announcing commencement of a new proceeding entitled *Determination of Royalty Rates for New Subscription Services for Digital Performance Right in Sound Recordings and Ephemeral Recordings*, Docket No. 14-CRB-0002-NSR (2016-2020) New Subscription III (the "NSS Proceeding") to determine royalty rates and terms applicable to the statutory licenses under Sections 112(e) and 114 of the Copyright Act for the period 2016 through 2020 for services of the type described in 37 C.F.R. § 383.2(h);

WHEREAS, the Parties are the only remaining participants in the NSS Proceeding; and

WHEREAS, the Parties wish to resolve all disputes relating to the NSS Proceeding, and believe it is beneficial to each Party to enter into an agreement that will obviate the need for the Parties to litigate against each other in the NSS Proceeding;

NOW, THEREFORE, in consideration of the mutual promises contained in this Agreement and for other good and valuable consideration, the adequacy and sufficiency of which are hereby acknowledged, the Parties hereby agree as follows:

1. Motion for Adoption of Settlement. The Parties agree to jointly file with the CRJs by no later than the next business day after the Execution Date a joint motion in the form of the Attachment to this Agreement (the "Motion for Adoption"), including the proposed regulations attached thereto as Exhibit A (the "Proposed Regulations"), notifying the CRJs that the Parties have reached a proposed settlement of the NSS Proceeding and requesting that it be adopted pursuant to 17 U.S.C. § 801(b)(7) and 37 C.F.R. § 351.2(b)(2).

2. Further Proceedings. Both Parties shall remain as participants in the NSS Proceeding until at least such time as the Proposed Regulations are adopted by the CRJs (whether in the form of the Proposed Regulations or otherwise) or rejected by the CRJs. Neither Party shall file a written direct statement in the NSS Proceeding (as currently required by December 12, 2014), except as may be reasonably required by action of the CRJs in the NSS Proceeding after the Execution Date. To the extent that further deadlines for action in the NSS Proceeding occur, the Parties shall cooperate with each other fully, and use commercially reasonable efforts, to take the minimal actions reasonably necessary or desirable to achieve adoption by the CRJs of the Proposed Regulations in their entirety as the determination in the NSS Proceeding. At no time shall either Party present a written direct statement or other argument or testimony, file a rate request or proposed findings of fact or conclusions of law, or take any other action, that in any such instance, is inconsistent with the Proposed Regulations, except as may be reasonably required by action of the CRJs in the NSS Proceeding after the

Execution Date. For the avoidance of doubt, if the CRJs reject the Proposed Regulations and set a new deadline for the filing of written direct statements, neither Party is precluded from filing a written direct statement and presenting testimony of its choosing, provided that such written direct statement and testimony shall not be inconsistent with the Proposed Regulations, except as may be reasonably required by action of the CRJs in the NSS Proceeding after the Execution Date. At no time shall either Party seek discovery from the other Party.

3. Mutual Representations. Each Party represents that it has the right, power and authority to enter into this Agreement and that this Agreement has been duly and validly executed by its authorized officer.

4. Agreement Non-Precedential. The royalty rates and terms set forth in the Proposed Regulations are intended to be nonprecedential in nature and based on the Parties' current understanding of market and legal conditions, among other things. Such royalty rates and terms shall be subject to *de novo* review and consideration in future proceedings. Such royalty rates and terms shall not be relied upon as precedent in any proceeding to set statutory royalty rates and terms (other than the NSS Proceeding).

5. Notices. All notices and other communications between the Parties shall be in writing and deemed received (a) when delivered in person (including by prepaid overnight courier); or (b) five (5) days after deposited in U.S. mails, postage prepaid, certified or registered mail, addressed to the other Party at the address set forth below (or such other address as such other Party may supply by written notice):

For SoundExchange:

General Counsel
SoundExchange, Inc.
733 10th Street N.W., 10th Floor
Washington, D.C. 20001
Phone: 202.640.5858

For Sirius XM:

Chief Financial Officer
Sirius XM Radio Inc.
1221 Avenue of the America
36th Floor
New York, NY 10020
Phone: 212.584.5100

With a copy to:

General Counsel
Sirius XM Radio Inc.
1221 Avenue of the America
36th Floor
New York, NY 10020
Phone: 212.584.5100

5. Counterparts. This Agreement may be executed in counterparts, including by means of facsimile or PDF transmission, each of which counterparts shall be deemed to be an original, but which taken together shall constitute one agreement.

6. Governing Law. This Agreement shall be governed by, and construed in accordance with, the laws of the District of Columbia (without giving effect to conflicts of law principles thereof).

7. Amendment. This Agreement may be modified or amended only by a writing signed by each of the Parties.

8. Entire Agreement. This Agreement represents the entire and complete agreement of the Parties and supersedes all prior and contemporaneous agreements and undertakings of the Parties with respect to the subject matter hereof.

IN WITNESS WHEREOF, the Parties have executed this Agreement as of the date first above written.

SOUNDEXCHANGE, INC.	SIRIUS XM RADIO INC.
By:	By:
Printed Name: C. Colin Rushing	Printed Name: David J. Frear
Title: SVP and General Counsel	Title: Executive Vice President and CFO
Date: December 11, 2014	Date: December 11, 2014

ATTACHMENT

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Washington, D.C.

In the Matter of: Determination of New Subscription Services Royalty Rates and Terms for Ephemeral Recording and Digital Performance of Sound Recordings	Docket No. 14-CRB-0002-NSR (2016-2020) (New Subscription III)

JOINT MOTION TO ADOPT SETTLEMENT

SoundExchange, Inc. ("SoundExchange") and Sirius XM Radio Inc. ("Sirius XM") (collectively, the "Parties") have reached a settlement of the above-captioned proceeding (the "Proceeding"). The Parties are pleased to submit the proposed regulatory language attached as Exhibit A (the "Settlement") for publication in the *Federal Register* for notice and comment in accordance with 17 U.S.C. § 801(b)(7)(A) and 37 C.F.R. § 351.2(b)(2). The Parties respectfully request that the Judges adopt the Settlement in its entirety as a settlement of rates and terms under Sections 112(e) and 114 of the Copyright Act for new subscription services of the type at issue in the Proceeding (*i.e.*, music services provided to residential subscribers as part of a cable or satellite television bundle).

I. Background

This Proceeding was instituted on January 3, 2014, for the purpose of determining royalty rates and terms under the Section 112(e) and 114 statutory licenses for the period 2016-2020 for the type of new subscription service defined in 37 C.F.R. § 383.2(h). 79 Fed. Reg. 410 (Jan. 3, 2014). Five entities filed petitions to participate: Music Reports, Inc. ("MRI"), the National Music Publishers' Association ("NMPA"), Sirius XM, Spotify USA, Inc. ("Spotify"), and

SoundExchange. The Judges struck the petitions to participate filed by MRI and NMPA, and Spotify withdrew from the Proceeding. As a result, Sirius XM and SoundExchange are the only remaining participants in this Proceeding.

SoundExchange is a nonprofit organization that is jointly controlled by representatives of sound recording copyright owners and performers. It has about 18,000 rights owner members and more than 40,000 artist members. The Copyright Royalty Judges have repeatedly designated SoundExchange as the collective to receive and distribute royalties under Sections 112(e) and 114 on behalf of all copyright owners and performers.

Sirius XM creates music and non-music programming and transmits it through its satellite digital audio radio service and other outlets. Sirius XM relies on the royalty rates and terms in 37 C.F.R. Part 383 for music programming it provides through the DiSH satellite television service. It is the only provider of a Part 383 service participating in this Proceeding.

II. Nature of the Settlement

The Settlement incorporates a simplified version of the royalty rate structure presently set forth in 37 C.F.R. Part 383. The Settlement maintains the per-subscriber fee structure, provides for annual 3% increases in the per-subscriber fee during the coming rate period, and eliminates the percentage of revenue prong of the rate calculation. In other respects, the Settlement preserves the existing provisions of Part 383 with only minor updating and technical and conforming changes.

III. Adoption of the Settlement by the Copyright Royalty Judges

The Copyright Royalty Judges have the authority "[t]o adopt as a basis for statutory terms and rates ... an agreement concerning such matters reached among some or all of the participants in a proceeding at any time during the proceeding" if other interested parties who "would be

bound by the terms, rates or other determination" set by the agreement are afforded "an opportunity to comment on the agreement." 17 U.S.C. § 801(b)(7)(A)(i). The Judges generally are required to adopt the rates and terms provided in such an agreement, unless a "participant [to the proceeding] objects to the agreement and the [Judges] conclude, based on the record before them if one exists, that the agreement does not provide a reasonable basis for setting statutory terms or rates." 78 Fed. Reg. 67,938, 67,939 (Nov. 13, 2013) (*Phonorecords II*) (quoting 17 U.S.C. § 801(b)(7)(A)(ii); alterations in original).

The Settlement is an agreement as described in 17 U.S.C. § 80l(b)(7)(A) reached between the only two participants remaining in the Proceeding. As a result, there is no basis for the Judges not to adopt the Settlement as the statutory terms and rates under Section 112(e) and 114 for services relying on the royalty rates and terms in 37 C.F.R. Part 383. Accordingly, the Parties respectfully request that the Judges publish the Settlement for notice and comment, and in due course adopt the Settlement in its entirety as the statutory rates and terms for such services.

Dated: December 11, 2014

Respectfully submitted,

Glenn D. Pomerantz (CA Bar 112503)
Kelly M. Klaus (CA Bar 161091)
Anjan Choudhury (DC Bar 497271)
MUNGER, TOLLES & OLSON LLP
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EXHIBIT A

PROPOSED REGULATIONS

The Parties propose that 37 C.F.R. Part 383 be revised to read as follows. (~~**Bold-strikethrough**~~ indicates language to be deleted and **bold underline** indicates language to be added.)

PART 383—RATES AND TERMS FOR SUBSCRIPTION TRANSMISSIONS AND THE REPRODUCTION OF EPHEMERAL RECORDINGS BY CERTAIN NEW SUBSCRIPTION SERVICES

Sec.

§ 383.1 General.

(a) *Scope.* This part 383 establishes rates and terms of royalty payments for the public performance of sound recordings in certain digital transmissions by Licensees in accordance with the provisions of 17 U.S.C. 114, and the making of certain ephemeral recordings by Licensees in accordance with the provisions of 17 U.S.C. 112(e), during the period commencing ~~**from the inception of the Licensees' Services**~~ **January 1, 2016** and continuing through December 31, ~~**2015**~~ **2020**.

(b) *Legal compliance.* Licensees relying upon the statutory licenses set forth in 17 U.S.C. 112(e) and 114 shall comply with the requirements of those sections and the rates and terms of this part.

(c) *Relationship to voluntary agreements.* Notwithstanding the royalty rates and terms established in this part, the rates and terms of any **voluntary** license agreements entered into by Copyright Owners and Licensees shall apply in lieu of the rates and terms of this part to transmissions with the scope of such agreements.

§ 383.2 Definitions.

For purposes of this part, the following definitions shall apply:

~~**(a) *Applicable Period* is the period for which a particular payment to the designated collection and distribution organization is due.**~~

(~~**b**~~**a**) *Bundled Contracts* means contracts between the Licensee and a Provider in which the Service is not the only content licensed by the Licensee to the Provider.

(eb) *Copyright Owner* is a sound recording copyright owner who is entitled to receive royalty payments made under this part pursuant to the statutory licenses under 17 U.S.C. 112(e) ~~or~~ and 114(~~g~~).

(dc) *License Period* means the period commencing ~~from the inception of the Licensees' Services~~ January 1, 2016 and continuing through December 31, ~~2015~~ 2020.

(ed) *Licensee* is a person that has obtained statutory licenses under 17 U.S.C. 112(e) and 114, and the implementing regulations, to make digital audio transmissions as part of a Service (as defined in paragraph (hf) of this section), and ephemeral recordings for use in facilitating such transmissions.

(~~f~~e) *Provider* means a "multichannel video programming distributor" as that term is defined in 47 CFR 76.1000(e); notwithstanding such definition, for purposes of this part, a Provider shall include only a distributor of programming to televisions, such as a cable or satellite television provider.

~~(g) *Revenue.* (1) "Revenue" means all monies and other considerations, paid or payable, recognizable during the Applicable Period as revenue by the Licensee consistent with Generally Accepted Accounting Principles ("GAAP") and the Licensee's past practices, which is derived by the Licensee from the operation of the Service and shall be comprised of the following:~~

~~(i) Revenues recognizable by Licensee from Licensee's Providers and directly from residential U.S. subscribers for Licensee's Service;~~

~~(ii) Licensee's advertising revenues recognizable from the Service (as billed), or other monies received from sponsors of the Service if any, less advertising agency commissions not to exceed 15% of those fees incurred to a recognized advertising agency not owned or controlled by Licensee;~~

~~(iii) Revenues recognizable for the provision of time on the Service to any third party;~~

~~(iv) Revenues recognizable from the sale of time to Providers of paid programming, such as infomercials, on the Service;~~

~~(v) Where merchandise, service, or anything of value is receivable by Licensee in lieu of cash consideration for the use of Licensee's Service, the fair market value thereof or Licensee's prevailing published rate, whichever is less;~~

~~(vi) Monies or other consideration recognizable as revenue by Licensee from Licensee's Providers, but not including revenues recognizable by Licensee's Providers from others and not accounted for by Licensee's Providers to Licensee, for the provision of hardware for the Service by anyone and used in connection with the Service;~~

~~(vii) Monies or other consideration recognizable as revenue for any references to or inclusion of any product or service on the Service; and~~

~~(viii) Bad debts recovered regarding paragraphs (g)(1)(i) through (vii) of this section.~~

~~(2) "Revenue" shall include such payments as set forth in paragraphs (g)(1)(i) through (viii) of this section to which Licensee is entitled but which are paid or payable to a parent, subsidiary, division, or affiliate of Licensee, in lieu of payment to Licensee but not including payments to Licensee's Providers for the Service. Licensee shall be allowed a deduction from "Revenue" as defined in paragraph (g)(1) of this section for bad debts actually written off during the reporting period.~~

(~~h~~f) A *Service* is a non-interactive (consistent with the definition of "interactive service" in 17 U.S.C. 114(j)(7)) audio-only subscription service (including accompanying information and graphics related to the audio) that is transmitted to residential subscribers of a television service through a Provider which is marketed as and is in fact primarily a video service where

(1) Subscribers do not pay a separate fee for audio channels.

(2) The audio channels are delivered by digital audio transmissions through a technology that is incapable of tracking the individual sound recordings received by any particular consumer.

(3) However, paragraph (~~h~~f)(2) of this section shall not apply to the Licensee's current contracts with Providers that are in effect as of the effective date of this part if such Providers become capable in the future of tracking the individual sound recordings received by any particular consumer, provided that the audio channels continued to be delivered to Subscribers by digital audio transmissions and the Licensee remains incapable of tracking the individual sound recordings received by any particular consumer.

(~~i~~g) *Subscriber* means every residential subscriber to the underlying service of the Provider who receives Licensee's Service in the United States for all or any part of a month; provided, however, that for any Licensee that is not able to track the number of subscribers on a per-day basis, "Subscribers" shall be calculated based on the average of the number of subscribers on the last day of the preceding month and the last day of the applicable month, unless the Service is paid by the Provider based on end-of-month numbers, in which event "Subscribers" shall be counted based on end-of-month data.

(~~j~~h) *Stand-Alone Contracts* means contracts between the Licensee and a Provider in which the only content licensed to the Provider is the Service.

§ 383.3 Royalty fees for public performances of sound recordings and the making of ephemeral recordings.

(a) *Royalty rates.* Royalty rates for the public performance of sound recordings by eligible digital transmissions made over a Service pursuant to 17 U.S.C. 114, and for ephemeral recordings of sound recordings made pursuant to 17 U.S.C. 112(e) to facilitate such transmissions during the

License Period, are as follows. Each Licensee will pay, with respect to content covered by the statutory ~~L~~licenses that is provided via the Service of each such Licensee:

(1) For Stand-Alone Contracts, ~~the greater of:~~

~~(i) 15% of Revenue, or~~

~~(ii) T~~the following monthly ~~minimum~~ payment per Subscriber to the Service of such Licensee—

~~(A) From inception through 2006: $0.0075~~

~~(B) 2007: $0.0075~~

~~(C) 2008: $0.0075~~

~~(D) 2009: $0.0125~~

~~(E) 2010: $0.0150~~

~~(F) 2011: $0.0155~~

~~(G) 2012: $0.0159~~

~~(H) 2013: $0.0164~~

~~(I) 2014: $0.0169~~

~~(J) 2015: $0.0174 and~~

(i) 2016: $0.0179;

(ii) 2017: $0.0185;

(iii) 2018: $0.0190;

(iv) 2019: $0.0196;

(v) 2020: $0.0202; and

(2) For Bundled Contracts, ~~the greater of:~~

~~(i) 15% of Revenue allocated to reflect the objective value of the Licensee's Service, or~~

~~(ii) T~~the following monthly ~~minimum~~ payment per Subscriber to the Service of such Licensee:

~~(A) From inception through 2006: $0.0220~~

~~(B) 2007: $0.0220~~

~~(C) 2008: $0.0220~~

~~(D) 2009: $0.0220~~

~~(E) 2010: $0.0250~~

~~(F) 2011: $0.0258~~

~~(G) 2012: $0.0265~~

~~(H) 2013: $0.0273~~

~~(I) 2014: $0.0281~~

~~(J) 2015: $0.0290~~

(i) 2016: $0.0299;

(ii) 2017: $0.0308;

(iii) 2018: $0.0317;

(iv) 2019: $0.0326;

(v) 2020: $0.0336.

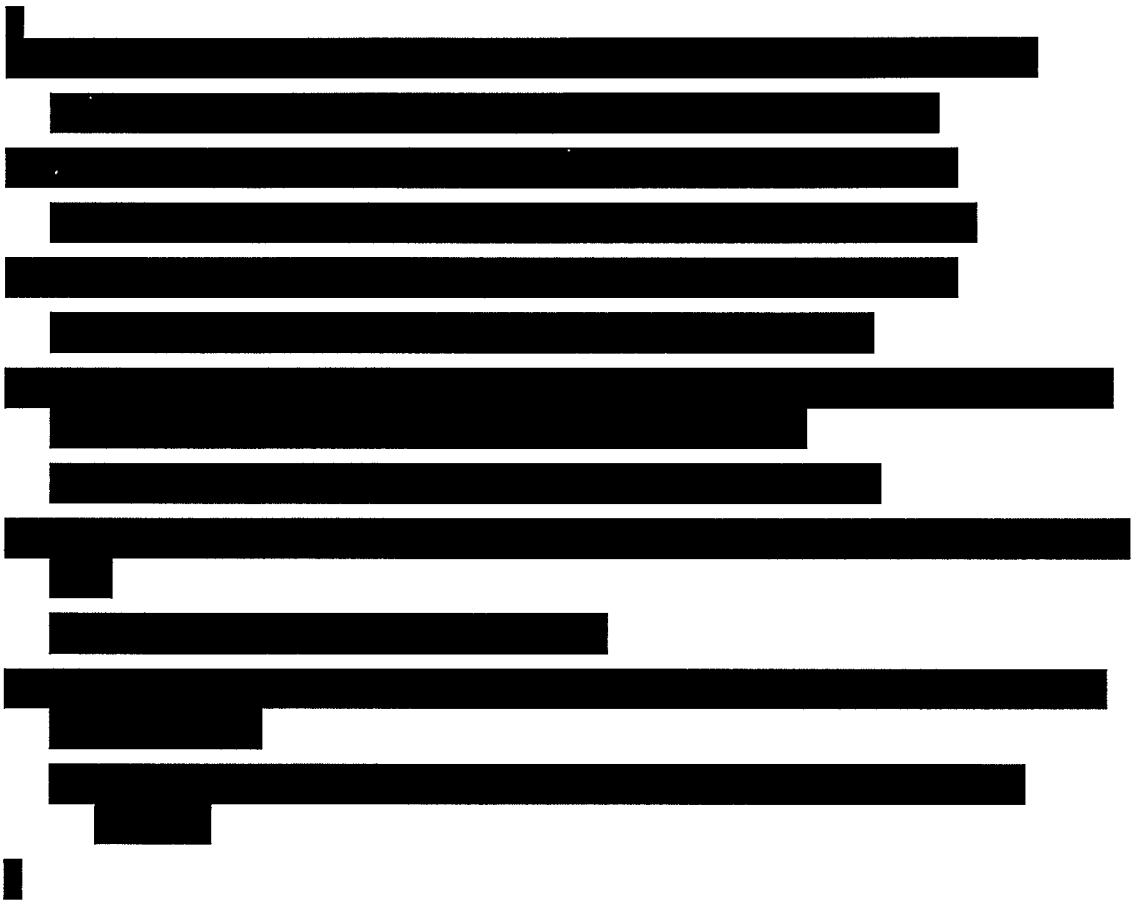
(b) *Minimum fee.* Each Licensee will pay an annual, non-refundable minimum fee of one hundred thousand dollars ($100,000), payable on January 31 of each calendar year in which the Service is provided pursuant to the section 112(e) and 114 statutory licenses~~, but payable pursuant to the applicable regulations for all years 2007 and earlier~~. Such fee shall be recoupable and credited against royalties due in the calendar year in which it is paid.

(c) *Ephemeral recordings.* The royalty payable under 17 U.S.C. 112(e) for the making of phonorecords used by the Licensee solely to facilitate transmissions during the License Period for which it pays royalties as and when provided in this part shall be included within, and constitute 5% of, such royalty payments.

§ 383.4 Terms for making payment of royalty fees.

(a) *Terms in general.* Subject to the provisions of this section, terms governing timing and due dates of royalty payments to the Collective, late fees, statements of account, audit and verification of royalty payments and distributions, cost of audit and verification, record retention

D.2. CABSAT Negotiation documents



Appendix E. Stingray webcasting activities documents

- In the Matter of: Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services, Docket No. 16-CRB-0001 SR/PSSR (208-2022), SoundExchange's Surreply in Opposition to Music Choice's Motion to Compel SoundExchange to Produce Documents and CABSAT Settlement Documents (Jan. 27, 2017)
- Exhibit A: Declaration of Brieanne Jackson (On behalf of SoundExchange)
- Exhibit B: Galaxie 2013 SoundExchange royalty statements
- Exhibit C: Galaxie 2014 SoundExchange royalty statements
- Exhibit D: Federal Register Public Notice of intention to audit Galaxie's (now called Stingray) New Subscription Service (CABSAT) and Business Establishment Service)

Appendix F. Materials Relied On

Music Choice and SoundExchange discovery documents and testimonies

- Rebuttal Testimony of David J. Del Beccaro and exhibits therein.
- Testimony of David J. Del Beccaro and exhibits therein.
- Testimony of Damon Williams and exhibits therein. Exhibit MC 15, Ipsos OTX MediaCT, Music Choice Viewership Study July 2015, 27, 35.
- January 10, 2005: Letter from Music Choice (David Del Beccaro, CEO) to Recording Industry Association of America (Steven M. Marks, Esq. General Counsel)
- June 14, 2005: Letter from RIAA (Steven M. Marks) to Music Choice (David Del Beccaro, CEO)
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- Music Choice Consolidated Financial Statements, 2013–2015. (MC0003221, MC0003130)
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- SoundX_000145804
- SoundX_000145808
- SoundX_000145813
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- SoundX_000477825, CABSAT Settlement Agreement.
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- SoundX_000477841-853. Attachment to email: Draft CABSAT Settlement Agreement, Nov. 26, 2014.
- SoundX_000477898-899. Email dated Dec. 3, 2014 4:56PM, Subject: FW: CABSAT III
- SoundX_000477900-912. Draft CABSAT Settlement Agreement, Nov. 26, 2014.
- SoundX_000477913-930. Draft CABSAT Settlement Agreement, Nov. 26, 2014.
- SoundX_000477980. Email dated Dec. 9, 2014 10:25PM, Subject: FW: CABSAT – Execution copy of settlement.
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- Warner Music Group, "Digital Strategy," Nov. 15, 2012, SX Ex. 011 (SoundX_000076302-330), 15 ,25.
- Warner Music Group, "Streaming Overview," Global Digital Summit, Jan. 2015, 7, 11 and 16. SoundX_000040364-380.

Copyright Royalty Board documents, statutes, and legal documents

- Before the Copyright Royalty Judges, Library of Congress, In the Matter of Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services, Docket No. 2011-1 CRB PSS/Satellite II, "Music Choice Proposed Findings of Fact," Sept. 26, 2012, ¶416 citing 6/14/12 Tr. 2152:10-2153:2 (Ciongoli). 6/14/12 Tr. 2165:15-2166:2 (Ciongoli).
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- In the Matter of: Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services, Docket No. 16-CRB-0001 SR/PSSR (2018-2022), SoundExchange's reply in Opposition to Music Choice's Motion to Compel SoundExchange to Produce Documents and CABSAT Settlement Documents (Jan. 27, 2017).
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Appendix G. Curriculum Vitae

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Education

Ph.D. in Economics, Stanford University, Stanford, CA, 1998
B.A., Economics (with Honors), University of Pennsylvania, Philadelphia, PA, 1991

Professional Experience

University of Zurich, Department of Economics

Professor of Applied Microeconomics, May 2013-current

Courses taught: *Graduate:* Structural Estimation in Applied Microeconomics (PhD), Empirical Industrial Organization (PhD), Cross-Section and Panel Data Econometrics (MSc)

Centre for Economic Policy Research (CEPR)

Co-Director, Industrial Organization Programme, September 2014-present
Research Fellow, Industrial Organization Programme, February 2011-present

Institute for Fiscal Studies (IFS)

International Research Fellow, August 2014-present

Centre for Competitive Advantage in the Global Economy (CAGE)

Research Fellow, April 2011-present

Association of Competition Economists (ACE)

Steering Committee, January 2016-present

University of Warwick, Department of Economics

Professor of Economics, September 2008-July 2013

Director of Research Impact, August 2012-July 2013
Director of Research, September 2009-July 2012
Courses taught: *Graduate:* Empirical Industrial Organization (MSc/PhD), Empirical Methods. *Undergraduate:* Introductory Econometrics (time series, limited dependent variables, panel data), Undergraduate Business Strategy.

Federal Communications Commission (FCC)

Chief Economist, September 2007 - August 2008

Reported to the then-FCC Chairman, Kevin Martin. Primary responsibilities were to advise the Chairman and his staff regarding the economic issues facing the Commission; to formulate and implement desired policies, to communicate and discuss these policies with senior Commission staff, and to assist as needed the 40+ staff economists. Main workstreams focused on the cable and satellite industries, including bundling and tying in wholesale and retail cable and satellite television markets and the economic analysis of XM/Sirius satellite radio merger. Also consulted on spectrum auction design, net neutrality, access pricing, ownership rules, and various international policy issues. Previous to joining the Commission, wrote a sponsored study analyzing media ownership and its impact in television markets.

University of Arizona, Department of Economics

Associate Professor of Economics, September 2008-August 2009 (on leave)
Assistant Professor of Economics, September 2002-August 2008 (on leave, 2007-08)

Courses taught: *Graduate:* Empirical Industrial Organization (2nd-year PhD), Business Strategy (MBA) *Undergraduate:* Introductory Econometrics (cross-section).

Duke University, Department of Economics

Assistant Professor of Economics, September 1997-August 2002

Courses taught: *Graduate:* Empirical Industrial Organization (2nd-year PhD), Graduate Econometrics (1st-year PhD), *Undergraduate:* Introductory Econometrics (cross-section), Introductory Microeconomics, The Economics and Statistics of Sports.

Other Academic Appointments

Visiting Professor, European School of Management and Technology, Berlin, Summer 2007.

Visiting Professor, Fuqua School of Business, Duke University, 2000-2001

Consulting Experience (Country)

Royalties for sound recording performance rights on cable television systems (US), 2016-present, testifying expert – Submitted direct and engaged to submit rebuttal testimony to copyright royalty judges on behalf of Music Choice regarding reasonable rates for sound recording performance rights on U.S. cable television systems.

Distribution of cable copyright royalties (US), 2014-present, testifying expert – Provided testimony to copyright royalty judges on behalf of the National Association of Broadcasters regarding relative market value of programming provided on the distant broadcast signals carried by U.S. cable systems.

A la carte offerings on pay television system (outside Europe), 2016, consulting expert – Advising pay-television operator regarding regulatory submission to require them to provide television channels on an a la carte basis.

Rules governing sale of football rights (EU), 2015-2016, consulting expert – Advised major pay-television distributor on regulatory filing challenging how rights are sold for a major European football league.

Geographic restrictions on sport TV broadcasts and Internet distribution (US), 2014-15, consulting expert – Advised on class-action lawsuit challenging geographic restrictions placed on member teams and regional sports networks regarding television broadcasts and Internet distribution by US sports leagues Major League Baseball (MLB) and the National Hockey League (NHL). Cases settled.

Royalties for sound recording performance rights by non-interactive webcasters (US), 2014-15, testifying expert – Prepared testimony for copyright royalty judges regarding reasonable rates for sound recording performance rights by a non-interactive webcaster. Client decided not to file a report.

Royalties for sound recording performance rights on cable television systems (US), 2011-12, testifying expert – Submitted direct and rebuttal testimony to copyright royalty judges on behalf of Music Choice regarding reasonable rates for sound recording performance rights on U.S. cable television systems. Testified before judge panel.

Evaluating "neighborhooding" of news channels on Comcast cable systems (US), 2011, lead expert – Designed and executed expert reports for complaint to FCC by Bloomberg (Television) L.P. (BTV) that Comcast was not fulfilling the neighborhooding conditions imposed during Comcast-NBCU merger. Defined news neighborhoods and investigated incidence of carriage of BTV on such neighborhoods. Compared patterns to neighborhooding of sports channels on Comcast and news channels on other operators and analyzed Comcast channel changes over time. Complaint largely granted by the FCC.

Evaluating switching costs in fixed voice telephony markets (UK), 2010-11, lead expert – Designed and executed reports for Office of Communication (Ofcom) evaluating the impact of automatically renewable ('rollover') contracts (ARCs) introduced by British Telecommunications (BT) in the UK fixed voice telephony market. Based on this analysis, Ofcom prohibited rollover contracts in all residential and small business fixed voice and broadband markets.

Evaluating competitive harms (US), 2010, consulting expert – Helped design and execute economic and econometric analyses in support of client opposed to major media merger. Analysis included market definition and quantifying the potential harms of the merger, including refusal to carry (foreclosure).

Analysis of advertising market regulations (UK), 2009-10, consulting expert – Advised project team on analysis of demand for advertising for the purpose of evaluating changes in regulation of advertising minutes on public-service broadcasters in the United Kingdom. Designed econometric model and supervised implementation and description of results. Report submitted to media regulator (Ofcom).

Distribution of cable copyright royalties (US), 2009-10, testifying expert – Submitted rebuttal testimony to copyright royalty judges regarding relative market value of programming provided on the distant broadcast signals carried by U.S. cable systems. Testified before judge panel.

Video chain merger (US), 2005, consulting expert – Supported lead expert in a challenge of a proposed merger of video chains. Merger denied.

Echostar/DirecTV (US), 2002-03, consulting expert – Supported analysis of liability for proposed merger. Helped design econometric model of pay-television demand and participated in conference calls with opposing lawyers and experts.

Plurimus / Foveon (US), 1999-00, consultant and advisory board member – Conducted market research and helped design business plan for Internet start-up seeking to enter the Internet audience measurement business. Projects included conducting a survey and strategic analysis of the early (June 1999) E-commerce market, presenting a framework for analyzing household choice (demand) on the Internet, conducting a strategic analysis of the company's business model, and advising on the design of the company's academic program. Company initially named Foveon; later renamed Plurimus.

Advisory roles:

Cartel case in the computer industry (US), 2009; German media market (Germany), 2007; Major price-fixing litigation (US), 1999-2001

Bates White LLC, Academic Affiliate, 2005-present

Publications

"The Economics of Television and Online Video Markets," Chapter 7 in Anderson, S., Waldfogel, J., and D. Stromberg, Handbook of Media Economics, volume 1A, 2015 Elsevier Press.

"Cable Regulation in the Internet Era," Chapter 3 in Rose, N., ed, "Economic Regulation and Its Reform: What Have We Learned?", 2014, University of Chicago Press.

"Accommodating Endogenous Product Choices: A Progress Report," *International Journal of Industrial Organization*, v30 (2012), 315-320.

"The Welfare Effects of Bundling in Multichannel Television Markets," (with Ali Yurukoglu), *American Economic Review*, v102n2 (April 2012), 643-685 (lead article).

"Price Discrimination in Service Industries," (with A. Lambrecht, K. Seim, N. Vilcassim, A. Cheema, Y. Chen, K. Hosanger, R. Iyengar, O. Koenigsberg, R. Lee, E. Miravete, and and O. Sahin), *Marketing Letters*, v23 (2012), 423-438.

"Economics at the FCC: 2007-2008," (with Evan Kwerel and Jonathan Levy), *Review of Industrial Organization*, v33n3 (November 2008), 187-210.

"The Discriminatory Incentives to Bundle: The Case of Cable Television," *Quantitative Marketing and Economics*, v6n1 (March 2008), 41-78.
- Winner, 2009 Dick Wittink Prize for the best paper published in the *QME*

"Bidding Asymmetries in Multi-Unit Auctions: Implications of Bid Function Equilibria in the British Spot Market for Electricity, (with Joseph Crespo and Helen Tauchen), *International Journal of Industrial Organization*, v25n6 (December 2007), 1233-1268.

"Bundling, Product Choice, and Efficiency: Should Cable Television Networks Be Offered A La Carte?," (with Joseph Cullen), *Information Economics and Policy*, v19n3-4 (October 2007), 379-404.

"Monopoly Quality Degradation and Regulation in Cable Television," (with Matthew Shum), *Journal of Law and Economics*, v50n1 (February 2007), 181-209.

"Uncertainty and Learning in Pharmaceutical Demand," (with Matthew Shum), *Econometrica*, v73n4 (July 2005), 1137-1174.

"Recent Advances in Structural Econometric Modeling: Dynamics, Product Positioning, and Entry," (with J.-P. Dube, K. Sudhir, A. Ching, M. Draganska, J. Fox, W. Hartmann, G. Hitsch, B. Viard, M. Villas-Boas, and N. Vilcassim), *Marketing Letters*, v16n2 (July 2005).

"The Impact of the 1992 Cable Act on Household Demand and Welfare," *RAND Journal of Economics*, v31n3 (Autumn 2000), 422-449.

Reports

"Empirical analysis of BT's automatically renewable contracts," (with ESMT Competition Analysis, Commissioned Research Study for the Office of Communications), August 2010. Also Supplementary Report, February 2011.

"Television Station Ownership Structure and the Quantity and Quality of TV Programming," (Commissioned Research Study for the Federal Communications Commission), July 2007.

Work in Progress

Articles Under Review

"The Welfare Effects of Vertical Integration in Multichannel Television Markets," (with Robin Lee, Michael Whinston, and Ali Yurukoglu), mimeo, University of Zurich, December 2015, revise and resubmit at *Econometrica.*

"Asymmetric Information and Imperfect Competition in Lending Markets," (with Nicola

Pavanini and Fabiano Schivardi), working paper, University of Zurich, April 2015, revise and resubmit at *American Economic Review.*

"The Welfare Effects of Monopoly Quality Choice: Evidence from Cable Television Markets," (with Matthew Shum and Alex Shcherbakov), mimeo, University of Zurich, August 2015, revise and resubmit at *American Economic Review.*

"The impact of 'rollover' contracts on switching in the UK voice market: Evidence from disaggregate customer billing data," (with Nicola Tosini and Keith Waehrer), Working paper, University of Warwick, June 2011, revise and resubmit at *Economic Journal.*

Working Papers

"Demand estimation with unobserved choice set heterogeneity," (with Rachel Griffith and Alessandro Iaria), University of Zurich, April 2016.

"The (inverse) demand for advertising in the UK: Should there be more advertising on television?," (with Jeremy Smith and Paul Sturgeon), working paper, University of Warwick, October 2011.

"The Empirical Consequences of Advertising Content in the Hungarian Mobile Phone Market," (with Jozsef Molnar), University of Arizona, March 2008.

Work In Progress

"Accommodating choice set heterogeneity in demand: Evidence from retail scanner data," (with Rachel Griffith and Alessandro Iaria), University of Warwick, October 2011.

"Orthogonal Instruments: Estimating Price Elasticities in the Presence of Endogenous Product Characteristics," (with Dan Ackerberg and Jin Hahn), mimeo, University of Warwick, June 2011.

"Channel 5 or 500? Vertical Integration, Favoritism, and Discrimination in Multichannel Television," (with Robin Lee, Breno Viera, Michael Whinston, and Ali Yurukoglu), mimeo, University of Zurich, October 2013.

"The Welfare Effects of Vertical Integration in Multichannel Television Markets," (with Robin Lee, Michael Whinston, and Ali Yurukoglu), mimeo, University of Zurich, March 2014.

Grants

"Endogenous Product Characteristics in Empirical Industrial Organization," Economic and Social Research Council, £140,000 (~$220,000), 2010-2012.

"The Empirical Consequences of Advertising Content" (with Jozsef Molnar), Hungarian Competition Commission, 10,000,000 Hungarian Forint (~$50,000), 2007-2008

Other Professional Activities

Editing/Refereeing

Associate Editor, *International Journal of Industrial Organization*, October 2005 - present.

Editorial Board, *Information Economics and Policy*, December 2007 - present.

Excellence in Refereeing Award, *American Economic Review*, 2009.

Referee for *Econometrica, American Economic Review, Review of Economics Studies, RAND Journal of Economics, Review of Economics and Statistics, Quantitative Marketing and Economics, National Science Foundation, International Journal of Industrial Organization, Journal of Industrial Economics, Journal of Applied Econometrics, Information Economics and Policy, Management Science, Southern Economic Journal*

Keynote Lectures (previous and planned)

"Vertical Integration in Media and Communications Markets": 5th Workshop on the Economics of ICTs (Oporto, Portugal, 3/14), FSR/EUI Annual Seminar on the Economics and Policy of Communications and Media 2014 (Florence, 3/14)

"How much is too much? A closer look at choice in the entertainment industry," The Future of Broadcasting Conference (London, 6/12)

Academic Presentations (previous and planned)

2016 Presentations: Winter Marketing-Economics Summit (Denver, 1/16), University of Bern (2/16), ESMT (Berlin, 6/16), Pompeu Fabra (Barcelona, 11,16)
2015 Presentations: NYC Media Seminar (2/15), Empirical Models of Differentiated Products (IFS, London, 6/15), Advances in the Economics of Antitrust and Consumer Protection (Paris, 9/15), University of Pennsylvania (Wharton, 9/15), 15th Media Economics Workshop (Cape Town, 11/15), Bocconi (12/15), ECARES (Brussels, 12/15)
2014 Presentations: Winter Marketing-Economics Summit (Wengen, Switzerland, 1/14), Industrieökonomischer Ausschuss (Hamburg, 2/14), Network of Industrial Economists (Manchester, UK, 10/14)
2013 Presentations: Tilburg University (11/13)
2012 Presentations: University of East Anglia / Centre for Competition Policy (5/12), PEDL Inaugural Conference (5/12)
2011 Presentations: University of Cyprus (3/11), CREST (Paris, 6/11), EARIE (Stockholm, 9/11), University of Zurich (9/11), University of Mannheim (10/11).
2010 Presentations: LBS (1/10), UCL (4/10), Oxford (5/10), Invitational Choice Conference (5/10), Manchester University (9/10), EIEF (Rome, 10/10), University of Venice (10/10), University College Dublin (11/10).
2009 Presentations: ESMT, Berlin (5/09), CEPR IO, Mannheim (5/09), University of Leuven (9/09), University of Toulouse (Econometrics Workshop and Competition Policy Workshop), (11/09)

Conference Organization:

CEPR Applied IO Workshop: Jerusalem (Hebrew University, 2017), London (IFS, 2016) Zurich (UZH,
EARIE 2010-2016: Scientific Committee
Economics of Media Markets 2010: Scientific Committee, Triangle Applied
Economics of Media Markets 2010: Scientific Committee, Triangle Applied
Micro Conference 2000: Organizer, Triangle
Applied Micro Conference 1999: Co-organizer

Non-Academic Presentations

"Damages Litigation: Issues and Challenges in Complex Antitrust Cases," CRESSE 2016 (Panel, Rhodes, 7/16)

"Multichannel Distribution: Experimentation, Innovation and Enforcement," CRA Conference on Economic Developments in European Competition Policy (Panel, Brussels, 12/15)

"Understanding 'New Media' and its lessons for non-media industries," University of Zurich Dept. of Economics, Advisory Board Meeting (Zürich, 11/13)

"New Media: Economic Perspectives," University of Warwick, Window on Research (Coventry, UK, 6/11)

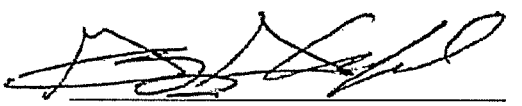
"Doing Good with (Good) Econometrics," Warwick Economics Summit, University of Warwick, (Coventry, UK, 2/11)

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Library of Congress
Washington, D.C.

In the Matter of:	Docket No. 16–CRB–0001–SR/PSSR (2018–2022)
Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and "Preexisting" Subscription Services (SDARS III)	

DECLARATION OF DR. GREGORY CRAWFORD, PH.D.,

I, Dr. Gregory Crawford, Ph.D., declare under penalty of perjury under the laws of the United States of America that the statements contained in my Written Rebuttal Testimony in the above-captioned matter are true and correct to the best of my knowledge, information, and belief. Executed this 16th day of October 2016 in Zurich, Switzerland.



Dr. Gregory Crawford, Ph.D.,

PUBLIC VERSION

MC 42

CONFIDENTIAL FOR SETTLEMENT PURPOSES

Execution Copy

CABSAT Settlement Agreement

This CABSAT Settlement Agreement ("Agreement"), dated as of December 11, 2014 (the "Execution Date"), is made by and between SoundExchange, Inc. ("SoundExchange") and Sirius XM Radio Inc. together with its subsidiaries (collectively "Sirius XM"). SoundExchange and Sirius XM are each referred to as a "Party" and collectively as the "Parties."

WHEREAS, the Copyright Royalty Judges ("CRJs") published in the Federal Register at 79 Fed. Reg. 410 (Jan. 3, 2014) a notice announcing commencement of a new proceeding entitled *Determination of Royalty Rates for New Subscription Services for Digital Performance Right in Sound Recordings and Ephemeral Recordings*, Docket No. 14-CRB-0002-NSR (2016-2020) New Subscription III (the "NSS Proceeding") to determine royalty rates and terms applicable to the statutory licenses under Sections 112(e) and 114 of the Copyright Act for the period 2016 through 2020 for services of the type described in 37 C.F.R. § 383.2(h);

WHEREAS, the Parties are the only remaining participants in the NSS Proceeding; and

WHEREAS, the Parties wish to resolve all disputes relating to the NSS Proceeding, and believe it is beneficial to each Party to enter into an agreement that will obviate the need for the Parties to litigate against each other in the NSS Proceeding;

NOW, THEREFORE, in consideration of the mutual promises contained in this Agreement and for other good and valuable consideration, the adequacy and sufficiency of which are hereby acknowledged, the Parties hereby agree as follows:

1. Motion for Adoption of Settlement. The Parties agree to jointly file with the CRJs by no later than the next business day after the Execution Date a joint motion in the form of the Attachment to this Agreement (the "Motion for Adoption"), including the proposed regulations attached thereto as Exhibit A (the "Proposed Regulations"), notifying the CRJs that the Parties have reached a proposed settlement of the NSS Proceeding and requesting that it be adopted pursuant to 17 U.S.C. § 801(b)(7) and 37 C.F.R. § 351.2(b)(2).

2. Further Proceedings. Both Parties shall remain as participants in the NSS Proceeding until at least such time as the Proposed Regulations are adopted by the CRJs (whether in the form of the Proposed Regulations or otherwise) or rejected by the CRJs. Neither Party shall file a written direct statement in the NSS Proceeding (as currently required by December 12, 2014), except as may be reasonably required by action of the CRJs in the NSS Proceeding after the Execution Date. To the extent that further deadlines for action in the NSS Proceeding occur, the Parties shall cooperate with each other fully, and use commercially reasonable efforts, to take the minimal actions reasonably necessary or desirable to achieve adoption by the CRJs of the Proposed Regulations in their entirety as the determination in the NSS Proceeding. At no time shall either Party present a written direct statement or other argument or testimony, file a rate request or proposed findings of fact or conclusions of law, or take any other action, that in any such instance, is inconsistent with the Proposed Regulations, except as may be reasonably required by action of the CRJs in the NSS Proceeding after the

Execution Date. For the avoidance of doubt, if the CRJs reject the Proposed Regulations and set a new deadline for the filing of written direct statements, neither Party is precluded from filing a written direct statement and presenting testimony of its choosing, provided that such written direct statement and testimony shall not be inconsistent with the Proposed Regulations, except as may be reasonably required by action of the CRJs in the NSS Proceeding after the Execution Date. At no time shall either Party seek discovery from the other Party.

3. Mutual Representations. Each Party represents that it has the right, power and authority to enter into this Agreement and that this Agreement has been duly and validly executed by its authorized officer.

4. Agreement Non-Precedential. The royalty rates and terms set forth in the Proposed Regulations are intended to be nonprecedential in nature and based on the Parties' current understanding of market and legal conditions, among other things. Such royalty rates and terms shall be subject to *de novo* review and consideration in future proceedings. Such royalty rates and terms shall not be relied upon as precedent in any proceeding to set statutory royalty rates and terms (other than the NSS Proceeding).

5. Notices. All notices and other communications between the Parties shall be in writing and deemed received (a) when delivered in person (including by prepaid overnight courier); or (b) five (5) days after deposited in U.S. mails, postage prepaid, certified or registered mail, addressed to the other Party at the address set forth below (or such other address as such other Party may supply by written notice):

For SoundExchange:

General Counsel
SoundExchange, Inc.
733 10th Street N.W., 10th Floor
Washington, D.C. 20001
Phone: 202.640.5858

For Sirius XM:

Chief Financial Officer
Sirius XM Radio Inc.
1221 Avenue of the America
36th Floor
New York, NY 10020
Phone: 212.584.5100

With a copy to:

General Counsel
Sirius XM Radio Inc.
1221 Avenue of the America
36th Floor
New York, NY 10020
Phone: 212.584.5100

5. Counterparts. This Agreement may be executed in counterparts, including by means of facsimile or PDF transmission, each of which counterparts shall be deemed to be an original, but which taken together shall constitute one agreement.

6. Governing Law. This Agreement shall be governed by, and construed in accordance with, the laws of the District of Columbia (without giving effect to conflicts of law principles thereof).

7. Amendment. This Agreement may be modified or amended only by a writing signed by each of the Parties.

8. Entire Agreement. This Agreement represents the entire and complete agreement of the Parties and supersedes all prior and contemporaneous agreements and undertakings of the Parties with respect to the subject matter hereof.

IN WITNESS WHEREOF, the Parties have executed this Agreement as of the date first above written.

SOUNDEXCHANGE, INC.

By: _____

Printed Name: C. Colin Rushing

Title: SVP and General Counsel

Date: December 11, 2014

SIRIUS XM RADIO INC.

By: _____

Printed Name: David J. Frear

Title: Executive Vice President and CFO

Date: December 11, 2014

ATTACHMENT

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Washington, D.C.

In the Matter of: Determination of New Subscription Services Royalty Rates and Terms for Ephemeral Recording and Digital Performance of Sound Recordings	Docket No. 14-CRB-0002-NSR (2016-2020) (New Subscription III)

JOINT MOTION TO ADOPT SETTLEMENT

SoundExchange, Inc. ("SoundExchange") and Sirius XM Radio Inc. ("Sirius XM") (collectively, the "Parties") have reached a settlement of the above-captioned proceeding (the "Proceeding"). The Parties are pleased to submit the proposed regulatory language attached as Exhibit A (the "Settlement") for publication in the *Federal Register* for notice and comment in accordance with 17 U.S.C. § 801(b)(7)(A) and 37 C.F.R. § 351.2(b)(2). The Parties respectfully request that the Judges adopt the Settlement in its entirety as a settlement of rates and terms under Sections 112(e) and 114 of the Copyright Act for new subscription services of the type at issue in the Proceeding (*i.e.*, music services provided to residential subscribers as part of a cable or satellite television bundle).

I. Background

This Proceeding was instituted on January 3, 2014, for the purpose of determining royalty rates and terms under the Section 112(e) and 114 statutory licenses for the period 2016-2020 for the type of new subscription service defined in 37 C.F.R. § 383.2(h). 79 Fed. Reg. 410 (Jan. 3, 2014). Five entities filed petitions to participate: Music Reports, Inc. ("MRI"), the National Music Publishers' Association ("NMPA"), Sirius XM, Spotify USA, Inc. ("Spotify"), and

SoundExchange. The Judges struck the petitions to participate filed by MRI and NMPA, and Spotify withdrew from the Proceeding. As a result, Sirius XM and SoundExchange are the only remaining participants in this Proceeding.

SoundExchange is a nonprofit organization that is jointly controlled by representatives of sound recording copyright owners and performers. It has about 18,000 rights owner members and more than 40,000 artist members. The Copyright Royalty Judges have repeatedly designated SoundExchange as the collective to receive and distribute royalties under Sections 112(e) and 114 on behalf of all copyright owners and performers.

Sirius XM creates music and non-music programming and transmits it through its satellite digital audio radio service and other outlets. Sirius XM relies on the royalty rates and terms in 37 C.F.R. Part 383 for music programming it provides through the DiSH satellite television service. It is the only provider of a Part 383 service participating in this Proceeding.

II. Nature of the Settlement

The Settlement incorporates a simplified version of the royalty rate structure presently set forth in 37 C.F.R. Part 383. The Settlement maintains the per-subscriber fee structure, provides for annual 3% increases in the per-subscriber fee during the coming rate period, and eliminates the percentage of revenue prong of the rate calculation. In other respects, the Settlement preserves the existing provisions of Part 383 with only minor updating and technical and conforming changes.

III. Adoption of the Settlement by the Copyright Royalty Judges

The Copyright Royalty Judges have the authority "[t]o adopt as a basis for statutory terms and rates ... an agreement concerning such matters reached among some or all of the participants in a proceeding at any time during the proceeding" if other interested parties who "would be

bound by the terms, rates or other determination" set by the agreement are afforded "an opportunity to comment on the agreement." 17 U.S.C. § 801(b)(7)(A)(i). The Judges generally are required to adopt the rates and terms provided in such an agreement, unless a "participant [to the proceeding] objects to the agreement and the [Judges] conclude, based on the record before them if one exists, that the agreement does not provide a reasonable basis for setting statutory terms or rates." 78 Fed. Reg. 67,938, 67,939 (Nov. 13, 2013) (*Phonorecords II*) (quoting 17 U.S.C. § 801(b)(7)(A)(ii); alterations in original).

The Settlement is an agreement as described in 17 U.S.C. § 801(b)(7)(A) reached between the only two participants remaining in the Proceeding. As a result, there is no basis for the Judges not to adopt the Settlement as the statutory terms and rates under Section 112(e) and 114 for services relying on the royalty rates and terms in 37 C.F.R. Part 383. Accordingly, the Parties respectfully request that the Judges publish the Settlement for notice and comment, and in due course adopt the Settlement in its entirety as the statutory rates and terms for such services.

Dated: December 11, 2014

Respectfully submitted,

Glenn D. Pomerantz (CA Bar 112503)
Kelly M. Klaus (CA Bar 161091)
Anjan Choudhury (DC Bar 497271)
MUNGER, TOLLES & OLSON LLP
355 S. Grand Avenue, 35th Floor
Los Angeles, CA 90071-1560
Telephone: (213) 683-9100
Facsimile: (213) 687-3702
Glenn.Pomerantz@mto.com
Kelly.Klaus@mto.com
Anjan.Choudhury@mto.com

Counsel for SoundExchange, Inc.

Counsel for Sirius XM Radio Inc.

EXHIBIT A

PROPOSED REGULATIONS

The Parties propose that 37 C.F.R. Part 383 be revised to read as follows. (~~**Bold strikethrough**~~ indicates language to be deleted and **bold underline** indicates language to be added.)

PART 383—RATES AND TERMS FOR SUBSCRIPTION TRANSMISSIONS AND THE REPRODUCTION OF EPHEMERAL RECORDINGS BY CERTAIN NEW SUBSCRIPTION SERVICES

Sec.

§ 383.1 General.

(a) *Scope.* This part 383 establishes rates and terms of royalty payments for the public performance of sound recordings in certain digital transmissions by Licensees in accordance with the provisions of 17 U.S.C. 114, and the making of certain ephemeral recordings by Licensees in accordance with the provisions of 17 U.S.C. 112(e), during the period commencing ~~**from the inception of the Licensees' Services**~~ **January 1, 2016** and continuing through December 31, ~~**2015**~~ **2020**.

(b) *Legal compliance.* Licensees relying upon the statutory licenses set forth in 17 U.S.C. 112(e) and 114 shall comply with the requirements of those sections and the rates and terms of this part.

(c) *Relationship to voluntary agreements.* Notwithstanding the royalty rates and terms established in this part, the rates and terms of any **voluntary** license agreements entered into by Copyright Owners and Licensees shall apply in lieu of the rates and terms of this part to transmissions with the scope of such agreements.

§ 383.2 Definitions.

For purposes of this part, the following definitions shall apply:

~~**(a) *Applicable Period* is the period for which a particular payment to the designated collection and distribution organization is due.**~~

(~~**b**~~**a**) *Bundled Contracts* means contracts between the Licensee and a Provider in which the Service is not the only content licensed by the Licensee to the Provider.

(eb) *Copyright Owner* is a sound recording copyright owner who is entitled to receive royalty payments made under this part pursuant to the statutory licenses under 17 U.S.C. 112(e) ~~or~~ and 114~~(g)~~.

(dc) *License Period* means the period commencing ~~from the inception of the Licensees' Services~~ January 1, 2016 and continuing through December 31, ~~2015~~ 2020.

(ed) *Licensee* is a person that has obtained statutory licenses under 17 U.S.C. 112(e) and 114, and the implementing regulations, to make digital audio transmissions as part of a Service (as defined in paragraph (hf) of this section), and ephemeral recordings for use in facilitating such transmissions.

(fe) *Provider* means a "multichannel video programming distributor" as that term is defined in 47 CFR 76.1000(e); notwithstanding such definition, for purposes of this part, a Provider shall include only a distributor of programming to televisions, such as a cable or satellite television provider.

~~(g) *Revenue.* (1) "Revenue" means all monies and other considerations, paid or payable, recognizable during the Applicable Period as revenue by the Licensee consistent with Generally Accepted Accounting Principles ("GAAP") and the Licensee's past practices, which is derived by the Licensee from the operation of the Service and shall be comprised of the following:~~

~~(i) Revenues recognizable by Licensee from Licensee's Providers and directly from residential U.S. subscribers for Licensee's Service;~~

~~(ii) Licensee's advertising revenues recognizable from the Service (as billed), or other monies received from sponsors of the Service if any, less advertising agency commissions not to exceed 15% of those fees incurred to a recognized advertising agency not owned or controlled by Licensee;~~

~~(iii) Revenues recognizable for the provision of time on the Service to any third party;~~

~~(iv) Revenues recognizable from the sale of time to Providers of paid programming, such as infomercials, on the Service;~~

~~(v) Where merchandise, service, or anything of value is receivable by Licensee in lieu of cash consideration for the use of Licensee's Service, the fair market value thereof or Licensee's prevailing published rate, whichever is less;~~

~~(vi) Monies or other consideration recognizable as revenue by Licensee from Licensee's Providers, but not including revenues recognizable by Licensee's Providers from others and not accounted for by Licensee's Providers to Licensee, for the provision of hardware for the Service by anyone and used in connection with the Service;~~

~~(vii) Monies or other consideration recognizable as revenue for any references to or inclusion of any product or service on the Service; and~~

~~(viii) Bad debts recovered regarding paragraphs (g)(1)(i) through (vii) of this section.~~

~~(2) "Revenue" shall include such payments as set forth in paragraphs (g)(1)(i) through (viii) of this section to which Licensee is entitled but which are paid or payable to a parent, subsidiary, division, or affiliate of Licensee, in lieu of payment to Licensee but not including payments to Licensee's Providers for the Service. Licensee shall be allowed a deduction from "Revenue" as defined in paragraph (g)(1) of this section for bad debts actually written off during the reporting period.~~

(**hf**) A *Service* is a non-interactive (consistent with the definition of "interactive service" in 17 U.S.C. 114(j)(7)) audio-only subscription service (including accompanying information and graphics related to the audio) that is transmitted to residential subscribers of a television service through a Provider which is marketed as and is in fact primarily a video service where

(1) Subscribers do not pay a separate fee for audio channels.

(2) The audio channels are delivered by digital audio transmissions through a technology that is incapable of tracking the individual sound recordings received by any particular consumer.

(3) However, paragraph (**hf**)(2) of this section shall not apply to the Licensee's current contracts with Providers that are in effect as of the effective date of this part if such Providers become capable in the future of tracking the individual sound recordings received by any particular consumer, provided that the audio channels continued to be delivered to Subscribers by digital audio transmissions and the Licensee remains incapable of tracking the individual sound recordings received by any particular consumer.

(**ig**) *Subscriber* means every residential subscriber to the underlying service of the Provider who receives Licensee's Service in the United States for all or any part of a month; provided, however, that for any Licensee that is not able to track the number of subscribers on a per-day basis, "Subscribers" shall be calculated based on the average of the number of subscribers on the last day of the preceding month and the last day of the applicable month, unless the Service is paid by the Provider based on end-of-month numbers, in which event "Subscribers" shall be counted based on end-of-month data.

(**jh**) *Stand-Alone Contracts* means contracts between the Licensee and a Provider in which the only content licensed to the Provider is the Service.

§ 383.3 Royalty fees for public performances of sound recordings and the making of ephemeral recordings.

(a) *Royalty rates.* Royalty rates for the public performance of sound recordings by eligible digital transmissions made over a Service pursuant to 17 U.S.C. 114, and for ephemeral recordings of sound recordings made pursuant to 17 U.S.C. 112(e) to facilitate such transmissions during the

License Period, are as follows. Each Licensee will pay, with respect to content covered by the statutory ~~L~~licenses that is provided via the Service of each such Licensee:

(1) For Stand-Alone Contracts, ~~the greater of:~~

~~(i) 15% of Revenue, or~~

~~(ii) T~~the following monthly ~~minimum~~ payment per Subscriber to the Service of such Licensee—

~~(A) From inception through 2006: $0.0075~~

~~(B) 2007: $0.0075~~

~~(C) 2008: $0.0075~~

~~(D) 2009: $0.0125~~

~~(E) 2010: $0.0150~~

~~(F) 2011: $0.0155~~

~~(G) 2012: $0.0159~~

~~(H) 2013: $0.0164~~

~~(I) 2014: $0.0169~~

~~(J) 2015: $0.0174 and~~

(i) 2016: $0.0179;

(ii) 2017: $0.0185;

(iii) 2018: $0.0190;

(iv) 2019: $0.0196;

(v) 2020: $0.0202; and

(2) For Bundled Contracts, ~~the greater of:~~

~~(i) 15% of Revenue allocated to reflect the objective value of the Licensee's Service, or~~

~~(ii) T~~the following monthly ~~minimum~~ payment per Subscriber to the Service of such Licensee:

~~(A) From inception through 2006: $0.0220~~

~~(B) 2007: $0.0220~~

~~(C) 2008: $0.0220~~

~~(D) 2009: $0.0220~~

~~(E) 2010: $0.0250~~

~~(F) 2011: $0.0258~~

~~(G) 2012: $0.0265~~

~~(H) 2013: $0.0273~~

~~(I) 2014: $0.0281~~

~~(J) 2015: $0.0290~~

(i) 2016: $0.0299;

(ii) 2017: $0.0308;

(iii) 2018: $0.0317;

(iv) 2019: $0.0326;

(v) 2020: $0.0336.

(b) *Minimum fee.* Each Licensee will pay an annual, non-refundable minimum fee of one hundred thousand dollars ($100,000), payable on January 31 of each calendar year in which the Service is provided pursuant to the section 112(e) and 114 statutory licenses~~, but payable pursuant to the applicable regulations for all years 2007 and earlier~~. Such fee shall be recoupable and credited against royalties due in the calendar year in which it is paid.

(c) *Ephemeral recordings.* The royalty payable under 17 U.S.C. 112(e) for the making of phonorecords used by the Licensee solely to facilitate transmissions during the License Period for which it pays royalties as and when provided in this part shall be included within, and constitute 5% of, such royalty payments.

§ 383.4 Terms for making payment of royalty fees.

(a) *Terms in general.* Subject to the provisions of this section, terms governing timing and due dates of royalty payments to the Collective, late fees, statements of account, audit and verification of royalty payments and distributions, cost of audit and verification, record retention

requirements, treatment of Licensees' confidential information, distribution of royalties by the Collective, unclaimed funds, designation of the Collective, and any definitions for applicable terms not defined herein and not otherwise inapplicable shall be those adopted by the Copyright Royalty Judges for subscription transmissions and the reproduction of ephemeral recordings by preexisting satellite digital audio radio services in 37 CFR part 382, subpart B of this chapter, for the license period ~~2007-2012~~ 2013-2017. For purposes of this section, the term "Collective" refers to the collection and distribution organization that is designated by the Copyright Royalty Judges. For the License Period through ~~2015~~ 2020, the sole Collective is SoundExchange, Inc.

(b) *Reporting of performances.* Without prejudice to any applicable notice and recordkeeping provisions, statements of account shall not require reports of performances.

(c) *Applicable regulations.* To the extent not inconsistent with this part, all applicable regulations, including part 370 of this chapter, shall apply to activities subject to this part.

MC 43-45
FILED UNDER SEAL

PUBLIC VERSION

MC 46

STEVEN M. MARKS
GENERAL COUNSEL

November 29, 2004

VIA FEDERAL EXPRESS

Mr. David Del Beccaro
President & Chief Executive Officer
Music Choice
110 Gibraltar Road
Suite 200
Horsham, PA 19044

Dear David:

I write to you regarding the launch of two new services by Music Choice, a new broadband offering and My MUSIC CHOICE. As discussed below, these new services are not eligible for the existing 7.25% rate, which is limited to preexisting subscription services of the type offered on July 31, 1998. Further, My MUSIC CHOICE appears to be an interactive service based on our understanding of how it functions, and it therefore requires Music Choice to obtain direct licenses from our members. The purpose of this letter is twofold: (1) to initiate discussions to establish an appropriate rate for Music Choice's new broadband service, and (2) to request that Music Choice promptly seek direct licenses for the new My MUSIC CHOICE service or provide us with information justifying its classification as a non-interactive service.

Music Choice on Broadband

Based on the description in Music Choice's press release of April 5, 2004, Music Choice's new broadband service offers "a content menu with a wide variety of options." Those options include the ability of a consumer to "select exclusive concerts, studio performances, and video interviews." The service also permits a consumer to "download the song or purchase the album." Consumers are also permitted to provide feedback and "identify ten of their favorite channels and store them under "My Channels."

Music Choice's new broadband service thus operates in a different medium than the service offered via cable or satellite television and grandfathered in the Digital Millennium Copyright Act of 1998 ("DMCA"), and includes functionality that takes

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advantage of new capabilities of the broadband medium. This functionality – including the ability of consumers to communicate back with the transmitting entity and receive additional, non-broadcast transmissions – was not available for transmissions via cable or satellite on July 31, 1998.

Both the statute and legislative history make clear that Music Choice's new broadband service does not qualify as a "preexisting subscription service." The statute says that a preexisting subscription service is one that "was in existence and was making such transmissions to the public for a fee on or before July 31, 1998." The legislative history to the DMCA explains that where a preexisting subscription service offers a "new service either in the same or new transmission medium by taking advantage of the capabilities of that medium, such new service *would not qualify as a preexisting subscription service.*" (emphasis added). Rather, the new service would be considered a new type of new subscription service. As such, the rates for the new service – even if made by a company that previously qualified as a preexisting subscription service – would be established under Section 114(f)(2)(B), which provides that the rates to be established are those "that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller," rather than under the Section 801(b) factors.

Because the Music Choice broadband service does not qualify as a preexisting subscription service, it is not eligible for the 7.25% rate established for such services. Instead, Music Choice must pay for the broadband service at some other rate. The rate established for new subscription webcasting could apply or a new rate may have to be established through a separate proceeding. Either way, we would like to speak with you in order to reach agreement that would avoid litigation or arbitration and marketplace uncertainty.

My MUSIC CHOICE

A January 12, 2004 press release describes My MUSIC CHOICE as a service that offers "*custom* music channels for digital cable subscribers." (Emphasis added). The release goes on to state that "My MUSIC CHOICE *enables its viewers to customize music channels* quickly and easily using their television remote to scroll through a few simple television screens that prompt them to choose the types of music by genre, set the mix of selected genres, and enter the name of their custom channel." (Emphasis added).

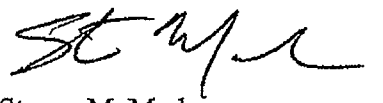
Based on this description, it would appear that the service makes transmissions that are "specially created" for each listener based on input from that listener. This fact would render My MUSIC CHOICE interactive and ineligible for statutory licensing. We therefore request that you promptly seek direct licenses from our member companies for this service.

If you believe that our view of the My MUSIC CHOICE service is mistaken, we encourage you to provide us with information demonstrating that this service is non-interactive. We note that even if the My MUSIC CHOICE service is non-interactive, it would not be a preexisting subscription service for the same reasons described above in the discussion of the broadband service. The two-way communication between the end user and Music Choice permitting the user to customize the genre mix delivered to such user renders the service a new type of new subscription service requiring a new rate.

Conclusion

Thank you in advance for your prompt attention to the matters raised in this letter. We and our members look forward to speaking with you further about Music Choice's new services, and working with you to bring consumers exciting ways to enjoy digital music.

Very truly yours,



Steven M. Marks

cc: Paula Calhoun
Fernando Laguarda

MUSIC CHOICE®

David J. Del Beccaro
President

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www.musicchoice.com

CONFIDENTIAL

VIA FACSIMILE & REGULAR MAIL

January 10, 2005

Steven M. Marks, Esq.
General Counsel
Recording Industry Association of America
1330 Connecticut Avenue, N.W., Suite 300
Washington, D.C. 20036

Dear Steve:

Thank you for your letter of November 29, 2004. As you know, Music Choice respects the rights of copyright owners and values its good relationship with your organization and its members. We have paid substantial royalties to sound recording copyright owners and complied with applicable reporting requirements and programming restrictions under the Copyright Act since they were first imposed in 1995. We appreciate the opportunity to update you on our program offerings.

The Music Choice residential audio service is a "preexisting subscription service" that performs sound recordings by means of non-interactive, audio-only subscription digital audio transmissions. The same service is transmitted to cable subscribers via satellite, cable headends, and cable infrastructure. Depending on how the signal is coded, it can be received through television set-top boxes or personal computers. The service has the same functionality whether delivered over the television or personal computer (i.e., an individual selects and listens to one channel at a time). The "broadband" description noted in your letter merely refers to the ability of cable listeners to receive the Music Choice audio channels over personal computers on a subscription basis, which has been possible since before July 31, 1998 and is not a change in the preexisting subscription service.

Music Choice does not offer personalized transmissions that are specially created for a particular recipient and are available only to some listeners but not to others. Music Choice does not allow listeners to select particular sound recordings or artists, or to skip, pause or rewind programming. Nothing about "My MUSIC CHOICE" alters or affects this in any way. Rather, it refers to the ability of listeners to select additional Music Choice channels as part of the preexisting subscription service. We do not believe that the provision of additional music channels, programmed in compliance with statutory restrictions (e.g., the "sound recording performance complement") and available to all listeners on the same subscription basis, gives rise to an "interactive service" under the Copyright Act or otherwise disqualifies the service as a preexisting subscription service.

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For these reasons, we are confident that Music Choice's preexisting subscription audio service complies with applicable law and is licensed. We hope that the foregoing information has clarified the issues raised in your letter. Please do not hesitate to contact me again if you have any further questions related to the above.

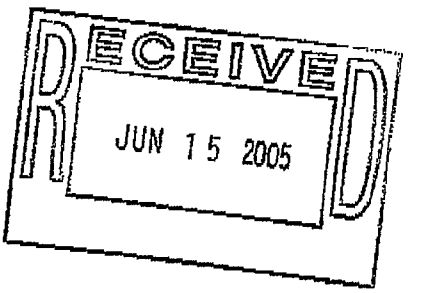
Sincerely,

David Del Beccaro

cc: Paula Calhoun, Esq.
Fernando Laguarda, Esq.

STEVEN M. MARKS
GENERAL COUNSEL

June 14, 2005



VIA FEDERAL EXPRESS

Mr. David Del Beccaro
President & Chief Executive Officer
Music Choice
110 Gibraltar Road
Suite 200
Horsham, PA 19044

Dear David:

I write to follow up on our earlier correspondence concerning two newer services being offered by Music Choice, a broadband service (the "Broadband Service") and My MUSIC CHOICE along with a brand new service, Music Choice for Mobile, that Music Choice is offering to Sprint's mobile phone service subscribers (the "Mobile Service"). (The three services mentioned above are collectively referred to below as the "New Services.") After reviewing your response with our member companies, we were unpersuaded by any of the arguments raised in your letter. As such, we now affirm the initial conclusion set forth in our earlier letter, namely, that none of the New Services qualify as a preexisting subscription service ("PES") and that none of them is eligible for the 7.25% royalty rate.

As explained more fully below, we have determined that the Broadband Service and the Mobile Service are both new subscription services and the My MUSIC CHOICE service is an interactive service, which is outside the statutory license altogether. Accordingly, the Broadband Service and the Mobile Service must immediately start making monthly royalty payments to SoundExchange at the applicable new subscription service rates and must each make lump-sum payments to SoundExchange no later than July 1, 2005 to cover the underpayment of royalties from each service's date of inception through the present. The My MUSIC CHOICE service must immediately remove all sound recordings owned by our member companies from the service unless and until the appropriate licenses are negotiated with our member companies.

The Broadband Service

As you know, the test for determining whether a new service qualifies as a PES is whether the transmissions at issue are similar in character to the transmissions that were being made by the licensee on or before July 31, 1998. Services that take advantage of

the capabilities of a particular medium, and services that offer video programming (other than information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording) do not qualify for treatment as a PES. See H.R. Conf. Rep. No. 796, 105th Cong., 2d Session at 89 (1998).

The Broadband Service clearly takes advantage of the capabilities of the broadband medium. It does so by, for example, offering users the ability to download or purchase music. It also offers video programming that goes far beyond that permitted under the legislative history (i.e. the videos provide more data than mere information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording.) For both of these reasons, the Broadband Service fails to qualify as a PES.

As such, the Broadband Service must begin calculating and paying monthly royalties to SoundExchange as of June 1, 2005 at the rates established for new subscription services (i.e., the new rate will be reflected in Music Choice's July 20 royalty payment to SoundExchange) and it must make a lump-sum payment to SoundExchange not later than July 1, 2005 to account for the shortfall in payments through May 31, 2005. This lump-sum payment should be equal to the difference between the payments already made by the Broadband Service at the PES rate and the amount the Broadband Service should have paid at the new subscription service rates since the inception of the Broadband Service.

As you may be aware, new subscription services currently have a choice of paying royalties at the rate of $.000762 per performance, $.0117 per aggregate tuning hour (for music intensive programming) or 10.9% of subscription service revenues (with a 27 cents per subscriber per month minimum). For further information about these rates and the applicable definitions, see 37 C.F.R. §§ 262.2, 262.3. These rates took effect as of January 1, 2003 and will remain in effect through December 31, 2005 (or until new rates are set for the 2006-2010 license period).

The Mobile Service

The Mobile Service fails to qualify as a PES for the same reasons as the Broadband Service. Like the Broadband Service, it takes advantage of the capabilities of the wireless medium by, for example, offering users on-demand access to Music Choice content and video programming (i.e., that is not merely information about the service, the sound recordings being transmitted or an advertisement to buy the sound recording.) As such, Music Choice may not pay royalties for the Mobile Service at the rates established for the PES.

Unlike the Broadband Service, the Mobile Service is not covered by the existing rates for new subscription services, as those rates were developed prior to the launch of any wireless music subscription services. However, in light of the fact that wireless services will presumably be covered by the rates established for the 2006-2010 license

period, our members would – for the sake of convenience – be willing to accept payment for the Mobile Service at the existing new subscription service rates for the period from the launch date of the Mobile Service through December 31, 2005.

As such, the Mobile Service must begin calculating and paying monthly royalties to SoundExchange as of June 1, 2005 at the rates established for new subscription services (i.e., the new rate will be reflected in Music Choice's July 20 royalty payment to SoundExchange) and it must make a lump-sum payment to SoundExchange not later than July 1, 2005 to account for the shortfall in payments through May 31, 2005. This lump-sum payment should be equal to the difference between the payments already made by the Mobile Service at the PES rate and the amount the Mobile Service would have paid, had it been paying at the new subscription service rates since its inception.

My MUSIC CHOICE

Based on further discussions with our members, we have concluded that the My MUSIC CHOICE service is interactive and is, therefore, ineligible for the statutory license. The statutory definition of an "interactive service" was amended in 1998 to make clear that "personalized transmissions -- those that are specially created for a particular individual—are to be considered interactive." Conference Report at 87. According to the (amended) statutory definition, an "interactive service" is one that "enables a member of the public to receive a transmission of a program specially created for the recipient, or on request, a transmission of a particular sound recording, whether or not as part of a program, which is selected by or on behalf of the recipient. . . ." 17 U.S.C. § 114(j)(7).

The fact that My MUSIC CHOICE users create personalized channels from preexisting, preprogrammed channels does not change the fact that the relative mix of preexisting channels comprising each user's custom channel is *specially created* by each individual user to suit his/her personal musical tastes. Nor does it matter that users are not permitted to select individual artists or tracks when creating their custom channel. Each user still ends up with a mixture of preprogrammed channels that is specially created by and for them. See Conference Report at 87 ("The recipient of the transmission need not select the particular recordings in the program for it to be considered personalized . . . .").

In light of our conclusion, we expect Music Choice to immediately commence negotiations with our member labels to obtain the licenses necessary to cover the transmissions made by the My MUSIC CHOICE service. Until such licenses are in place, Music Choice must either remove all sound recordings owned or controlled by our member companies from the My MUSIC CHOICE service or cease operating the service altogether.

Thank you in advance for your prompt attention to the matters raised in this letter. Please feel free to contact me if you have any questions about what Music Choice must do to comply with the terms of this letter.

We await your response.

Very truly yours,

Steven M. Marks

cc: Paula Calhoun
Fernando Laguarda

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CONFIDENTIAL
VIA FACSIMILE & REGULAR MAIL

June 30, 2005

Steven M. Marks, Esq.
General Counsel
Recording Industry Association of America
1330 Connecticut Avenue, N.W., Suite 300
Washington, D.C. 20036

Dear Steve:

This letter responds to your letter of June 14, 2005 concerning three services offered by Music Choice. One of these is a broadband residential audio service, another is the same service offered to Sprint's mobile phone service subscribers, and the third is the "My MC" offering. As to the first two, you assert they are not preexisting subscription services and thus are ineligible, in your opinion, for the 7.25% rate established for such services. As to the third, you assert it is an interactive service and as such ineligible for the statutory license. We have carefully reviewed your letter along with our earlier correspondence on this issue, and respectfully disagree.

Here's why. There is no doubt Music Choice is a preexisting service within the meaning of 17 U.S.C. §114(j)(11): the Conference Committee report on the DMCA expressly refers to us. H.R. Rep. No. 796, 105th Cong., 2d Sess. 89 (1998). It is also clear that Music Choice is not limited to the transmission medium in existence on July 31, 1998. The Conference Committee report says that the grandfathered rights extend to "any new services in a new transmission medium where only transmissions similar to the[] existing service are provided."

The report then gives the following, quite apposite example: "if a cable subscription music service making transmissions on July 31, 1998, were to offer the same music service through the Internet, then such Internet service would be considered part of a preexisting subscription service." We deliver the same audio music service as our cable subscription service over a closed network to cable subscribers' computers. If delivering such service over the Internet is considered part of the preexisting subscription service, as the report clearly states, then certainly our audio broadband service should be considered part of the preexisting subscription service.

The key to determining whether a preexisting service offered in a new medium qualifies for the preexisting service rate is *not* the nature of the medium or the fact that a new

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medium is employed (as you apparently assert) but, rather, as the report states, whether the content of the transmission is similar to the one in existence on July 31, 1998. Our broadband service is.

It is true that the committee report refers to "taking advantage of the capabilities" of a new transmission medium, but this language comes after the reference to the Internet – and thus cannot preclude using a new medium – and, moreover, the report then gives an example of what it does mean by this phrase: it gives the example of a service that post-July 31, 1998 begins offering "video programming, such as advertising or other content...."

What the report has in mind is a previously existing audio service that, due to new broadband capabilities, now offers a new type of transmission, that is audio programming mixed with video. But even this is allowed in some circumstances, as the report continues, so long as if the video programming contains information about the service, the sound recordings being transmitted, the artists, composers or songwriters or is an ad to purchase the sound recording.

In taking a contrary view from ours, we believe you misunderstand the nature of our service and Congress's intent. The music transmission as it existed before July 31, 1998 is the same now. We have not added video programming to it. We do offer video programming, but that is on a different transmission and is separately licensed. Although the interface for the broadband Music Choice service allows listeners to switch over to this other, separately licensed, service providing the video transmissions, we do not read the Act to preclude a service such as ours from doing so. Congress only intended to preclude us from including video programming into an existing audio transmission and then relying on the compulsory license for the now mixed transmission. Since audiovisual works aren't subject to compulsory licensing under Section 114, this makes sense: it prevents grandfathered services from distorting the compulsory license. But our music transmission isn't mixed: it is still pure audio, and as such it remains faithful to the compulsory license.

We are somewhat puzzled by your apparent reading of the statute. Under that reading, simply because we have to separately license our new video service at market rates, we must also pay higher rates for the same audio programming service as existed before July 31, 1998. In other words, you appear to be arguing that Music Choice must pay a higher fee for its preexisting audio programming service not because that service has changed materially – it has not – but solely because we now separately license video programming for a different transmission as part of a different service. Congress could not have intended that result. We therefore adhere to our position that we are entitled to the preexisting rate for the audio programming service.

This analysis applies equally to our wireless service. As with the broadband service, the wireless interface may allow users to also access other, separately licensed services, but the underlying Music Choice audio transmission service provides the same channels and

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programming as the original and broadband services. As long as the content transmitted by the wireless service is similar to the content provided by our preexisting service (and it is), Music Choice is entitled to rely on the preexisting rate.

The final issue is whether My MC is interactive. We believe you misunderstand the My MC portion of our audio service. As an initial matter, though, we are very surprised RIAA is concerned with our genre-based channels. In the LAUNCHcast litigation, the LAUNCHcast service offered genre channels, but those channels were not the basis of the suit and we understand RIAA may have taken the position that such stations do not make a service interactive. That makes perfect sense. Congress's concern with interactivity, found in the initial 1995 definition, was with displacement of sales: if a consumer could so influence what he or she heard that there was no need to buy a sound recording, the record company lost a sale. That is not true for genre stations, which instead boost consumer awareness of performers and therefore increase sales.

In any event, nothing in the 1998 amendment to the definition of "interactive service" changes the result for our service. While we recognize that a certain reading of our marketing materials, without an understanding of how the service actually works, might have given you the wrong impression, it is simply not true that there is a custom channel for any user. All users who select the same mix of genres hear the same music at the same time. Music Choice has created a pre-programmed channel for every permutation of possible mixes of genres. When a user selects a particular mix of genres, that user is served an audio transmission that Music Choice, not the user, has selected. Where more than one user selects the same mix of genres, all such users will receive the same transmission and at the same time. Contrary to your letter, no user "ends up with a mixture of preprogrammed channels that is specifically created by and for them."

In light of the further explanation, above, of how our services actually function, we re-iterate our position that the audio programming services we offer via broadband and wireless media fall within the statutory license for pre-existing services because they offer the same programming as Music Choice's cable service. The My MC portion of our service is non-interactive because no program is ever specially created for an individual user. Instead, all users who select the same blend of genres hear the same program at the same time. We trust this resolves the matter and that the labels will be pleased that we are continuing to provide them with exposure for their artists.

Sincerely,

David Del Beccaro

cc: Paula Calhoun, Esq.

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PUBLIC VERSION

MC 47

Stingray Music Brings All Good Vibes to AT&T U-verse Customers

AT HOME / Montreal, Quebec, and Dallas, Texas, Oct 29, 2014

MONTREAL / DALLAS, Oct. 29, 2014 – Stingray, the leading global provider of multiplatform musical services for Pay TV operators, and AT&T* U-verse®, announced the launch of Stingray Music, a new music app available on U-verse TV. The app is available to U-verse TV customers with U-verse High Speed Internet on channels 531/1531 or by selecting Go Interactive on a U-verse TV remote.

The new **Stingray Music** app, available at no additional charge, will have more than 100 streaming music channels and thousands of videos across all popular music genres. Customers can select from a wide variety of top channels including Hit List, Rock, Hot Country, Pop, Hip Hop, Latino Tropical and more. The **Stingray Music** app offers ad-free streaming, high quality digital audio, channels curated by music experts from around the world, and access to the latest releases and chart-topping artists.

Coming next March, subscribers will also see 75 new music channels appear in their TV listing with direct access to the **Stingray Music** app. More music, greater variety, total new experience!

"We are honored that AT&T U-verse has chosen to offer this interactive music and video feature to its customers," stated Eric Boyko, President and CEO of Stingray. "With Stingray Music, AT&T U-verse customers get the best music for every moment, place and mood in their life. The launch of the Stingray Music app creates a universe of unlimited options for them and the possibility to have a tailored music experience that fits their tastes."

"We're always looking for ways to make the U-verse experience more interactive," said Mel Coker, chief marketing officer, AT&T Home Solutions. "Stingray Music is a perfect fit for our extensive list of interactive apps that help customers engage and have more fun with their U-verse TV experience."

Stingray Music is the latest interactive TV app available for AT&T U-verse customers. TV apps and multi-screen services help drive U-verse customer engagement, satisfaction and growth. AT&T U-verse TV has 6.1 million subscribers and now has annualized total revenues of $15 billion***. For additional information on AT&T U-verse — or to find out if it's available in your area — visit www.att.com/u-verse.

Geographic and service restrictions apply to AT&T U-verse services. Call or go to www.att.com/u-verse to see if you qualify.

*AT&T products and services are provided or offered by subsidiaries and affiliates of AT&T Inc. under the AT&T brand and not by AT&T Inc.

** Requires U-verse Internet Elite or higher. Stingray Music USA Inc.'s terms and conditions apply.

*** As of 3Q2014.

About AT&T

AT&T Inc. (NYSE:T) is a premier communications holding company and one of the most honored companies in the world. Its subsidiaries and affiliates – AT&T operating companies – are the providers of AT&T services in the United States and internationally. With a powerful array of network resources that includes the nation's most reliable 4G LTE network, AT&T is a leading provider of wireless, Wi-Fi, high speed Internet, voice and cloud-based services. A leader in mobile Internet, AT&T also offers the best global wireless coverage, based on offering roaming in more countries than any other U.S. based carrier, and offers the most wireless phones that work in the most countries. It also offers advanced TV service with the AT&T U-verse® brand. The company's suite of IP-based business communications services is one of the most advanced in the world.

Additional information about AT&T Inc. and the products and services provided by AT&T subsidiaries and affiliates is available at http://about.att.com or follow our news on Twitter at @ATT, on Facebook at http://www.facebook.com/att and YouTube at http://www.youtube.com/att.

Reliability claim based on analysis of independent third party data re nationwide carriers' 4G LTE. LTE is a trademark of ETSI. 4G LTE not available everywhere.

About Stingray

Stingray is the leading multi-platform music service provider in the world, with more than 110 million subscribers in 113 countries around the world. Geared towards individuals and businesses alike, the company's commercial entities

include leading digital music and video services Stingray Music, Stingray Concerts, Stingray Music Videos, and Stingray Karaoke. The company also offers various business solutions, including music or digital display based solutions through its Stingray Business division.

Majority-owned by Telesystem, Novacap and Boyko Investment Corporation, Stingray is headquartered in Montreal and has over 200 employees in offices across Canada, as well as additional offices in Los Angeles, Miami, London, Amsterdam, and Tel Aviv. The company stood out in 2013 by ranking 15th on Deloitte's Technology Fast 50MC list, and figuring amongst PROFIT magazine's fastest growing Canadian companies. For more information, please visit www.stingray.com.

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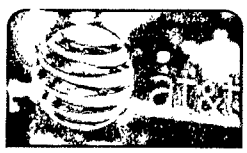
AT&T Fiber



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PUBLIC VERSION

MC 48

Stingray Music Channel Lineup on AT&T U-verse TV

U-verse TV Channel	Stingray Station	Media Room Genre	Rating
5100	Stingray Greatest Hits	Pop	TV-14
5101	Stingray Hit List	Pop	TV-14
5102	Stingray Dance Clubbin'	Dance	TV-MA
5103	Stingray Eclectic Electronic	Dance	TV-MA
5104	Stingray Alt Rock Classics	Rock	TV-14
5105	Stingray Hip Hop	Urban	TV-MA
5106	Stingray Urban Beats	Urban	TV-MA
5107	Stingray Classic R'n'B & Soul	Urban	TV-14
5108	Stingray Groove (Disco & Funk)	Urban	TV-14
5109	Stingray Retro R&B	Urban	TV-14
5110	Stingray Soul Storm	Urban	TV-14
5111	Stingray Gospel	Extra	TV-PG
5112	Stingray Jammin'	Multi-cultural	TV-14
5113	Stingray Rock	Rock	TV-MA
5114	Stingray Heavy Metal	Rock	TV-MA
5115	Stingray Rock Alternative	Rock	TV-MA
5116	Stingray Adult Alternative	Rock	TV-MA
5117	Stingray Rock Anthems	Rock	TV-14
5118	Stingray Classic Rock	Rock	TV-14
5119	Stingray Pop Adult	Pop	TV-14
5120	Stingray Freedom	Pop	TV-14
5121	Stingray Maximum Party	Pop	TV-14
5122	Stingray Popcorn	Extra	TV-PG
5123	Stingray OMG	Pop	TV-G
5124	Stingray Kids' Stuff	Extra	TV-Y
5125	Stingray Y2K	Decades	TV-14
5126	Stingray Nothin' but '90s	Decades	TV-14
5127	Stingray Remember the '80s	Decades	TV-14
5128	Stingray Flashback '70s	Decades	TV-14
5129	Stingray Jukebox Oldies	Decades	TV-14
5130	Stingray Alt-Country Americana	Country	TV-14
5131	Stingray Hot Country	Country	TV-14
5132	Stingray No Fences	Country	TV-14
5133	Stingray Country Classics	Country	TV-PG
5134	Stingray The Light	Pop	TV-PG
5135	Stingray Today's Latin Pop	Latin	TV-14
5136	Stingray Latino Urbana	Latin	TV-MA
5137	Stingray Retro Latino	Latin	TV-PG
5138	Stingray Latino Tropical	Latin	TV-14
5139	Stingray Holiday Hits	Extra	TV-14
5140	Stingray The Spa	Extra	TV-G
5141	Stingray Smooth Jazz	Jazz	TV-PG
5142	Stingray Jazz Masters	Jazz	TV-PG
5143	Stingray The Blues	Jazz	TV-14
5144	Stingray Swinging Standards	Jazz	TV-14
5145	Stingray Easy Listening	Pop	TV-G
5146	Stingray Pop Classics	Classical	TV-G
5147	Stingray '60s	Decades	TV-G
5148	Stingray Southern Jams	Rock	TV-14
5149	Stingray Bluegrass	Country	TV-G
5150	Stingray Silk (Love Songs)	Pop	TV-14
5151	Stingray New Age	Extra	TV-G
5152	Stingray Trance	Dance	TV-MA
5153	Stingray Romance Latino	Latin	TV-14
5154	Stingray Rock en Español	Latin	TV-14
5155	Stingray Salsa/Merengue	Latin	TV-14
5156	Stingray Solo Para Peques	Latin	TV-G
5157	Stingray Samba & Pagode	Latin	TV-G
5158	Stingray Tagalog	Multi-cultural	TV-14
5159	Stingray Bollywood Hits	Multi-cultural	TV-14
5160	Stingray Classical India	Multi-cultural	TV-PG
5161	Stingray Hindi Gold	Multi-cultural	TV-14
5162	Stingray Punjabi	Multi-cultural	TV-14
5163	Stingray Sounds of South India	Multi-cultural	TV-14
5164	Stingray Arabian Nights	Multi-cultural	TV-G
5165	Stingray Farsi	Multi-cultural	TV-14
5166	Stingray Guangdong	Multi-cultural	TV-14
5167	Stingray Asian Hits	Multi-cultural	TV-14

Browse our Stingray Music genre selections on **channels 5100-5174** and press **OK** on your U-verse TV remote to begin listening. Or press **Go Interactive** or tune to **Ch. 531/1531 HD** to search within the Stingray Music app for the best music for every moment, place, and mood in your life.

Stingray Music Channel Lineup on AT&T U-verse TV

U-verse TV Channel	Stingray Station	Media Room Genre	Rating
5168	Stingray Mando Popular	Multi-cultural	TV-14
5169	Stingray Euro Hits	Pop	TV-14
5170	Stingray Franco Pop	Pop	TV-14
5171	Stingray Total Hits - France	World Music	TV-14
5172	Stingray Total Hits - Italy	World Music	TV-14
5173	Stingray Total Hits - Russia	World Music	TV-14
5174	Stingray Total Hits - Poland	World Music	TV-14
App Only	Stingray Baroque	Classical	TV-G
App Only	Stingray Classic Masters	Classical	TV-G
App Only	Stingray Chamber Music	Classical	TV-G
App Only	Stingray Opera Plus	Classical	TV-G
App Only	Stingray Broadway	Classical	TV-G
App Only	Stingray Türk Sanat Müziği	Classical	TV-G
App Only	Stingray Franco Country	Country	TV-PG
App Only	Stingray Folk Roots	Country	TV-PG
App Only	Stingray Dancehall Session	Dance	TV-14
App Only	Stingray Soca Motion	Dance	TV-PG
App Only	Stingray Reggaeton	Dance	TV-MA
App Only	Stingray Dance Classics	Dance	TV-PG
App Only	Stingray House	Dance	TV-14
App Only	Stingray Alternative Dance	Dance	TV-14
App Only	Stingray Bass, Breaks & Beats	Dance	TV-14
App Only	Stingray Nostalgie	Decades	TV-G
App Only	Stingray Rewind ('80s & '90s)	Decades	TV-G
App Only	Stingray Revival ('60s & '70s)	Decades	TV-G
App Only	Stingray Nature	Extra	TV-Y
App Only	Stingray The Chill Lounge	Extra	TV-G
App Only	Stingray South Africa Gospel	Extra	TV-G
App Only	Stingray East African Gospel	Extra	TV-G
App Only	Stingray Franco Fêtes	Extra	TV-G
App Only	Stingray Holiday Favorites	Extra	TV-G
App Only	Stingray Jazz Now	Jazz	TV-PG
App Only	Stingray Big Band	Jazz	TV-PG
App Only	Stingray Cocktail Lounge	Jazz	TV-G
App Only	Stingray Cool Jazz	Jazz	TV-G
App Only	Stingray Jazz Latino	Latin	TV-G
App Only	Stingray Latino Tejano	Latin	TV-G
App Only	Stingray Regional Mexican	Latin	TV-PG
App Only	Stingray Brazilian Pop	Latin	TV-PG
App Only	Stingray Latin Lounge	Latin	TV-G
App Only	Stingray Tango	Latin	TV-14
App Only	Stingray Mariachi Forever	Latin	TV-G
App Only	Stingray Caribbean Vintage Vibes	Multi-cultural	TV-PG
App Only	Stingray Hellenic Sounds	Multi-cultural	TV-G
App Only	Stingray Afro Beat	Multi-cultural	TV-G
App Only	Stingray La Vita è Bella	Multi-cultural	TV-G
App Only	Stingray World Carnival	Multi-cultural	TV-G
App Only	Stingray South Africa Traditional	Multi-cultural	TV-PG
App Only	Stingray Nederpop	Multi-cultural	TV-14
App Only	Stingray Franco Attitude	Rock	TV-MA
App Only	Stingray Canadian Indie	Rock	TV-MA
App Only	Stingray Headbangers	Rock	TV-MA
App Only	Stingray Hard Rock	Rock	TV-MA
App Only	Stingray Brazil Rock	Rock	TV-PG
App Only	Stingray Indie Classics	Rock	TV-PG
App Only	Stingray Motown	Urban	TV-G
App Only	Stingray Total Hits - Brazil	World Music	TV-PG
App Only	Stingray Hungarian Pop & Rock	World Music	TV-PG
App Only	Stingray Total Hits - UK	World Music	TV-PG
App Only	Stingray Total Hits - Germany	World Music	TV-PG
App Only	Stingray Total Hits - Spain	World Music	TV-PG
App Only	Stingray Total Hits - Netherlands	World Music	TV-PG
App Only	Stingray Total Hits - Belgium	World Music	TV-PG
App Only	Stingray Total Hits - Switzerland	World Music	TV-PG
App Only	Stingray Hot in South Africa	World Music	TV-PG
App Only	Stingray Hot in Germany	World Music	TV-PG
App Only	Stingray Total Hits - Austria	World Music	TV-PG
App Only	Stingray Hot in Norway	World Music	TV-PG

PUBLIC VERSION

MC 49

(https://www.riaa.com/)

U.S. SALES DATABASE

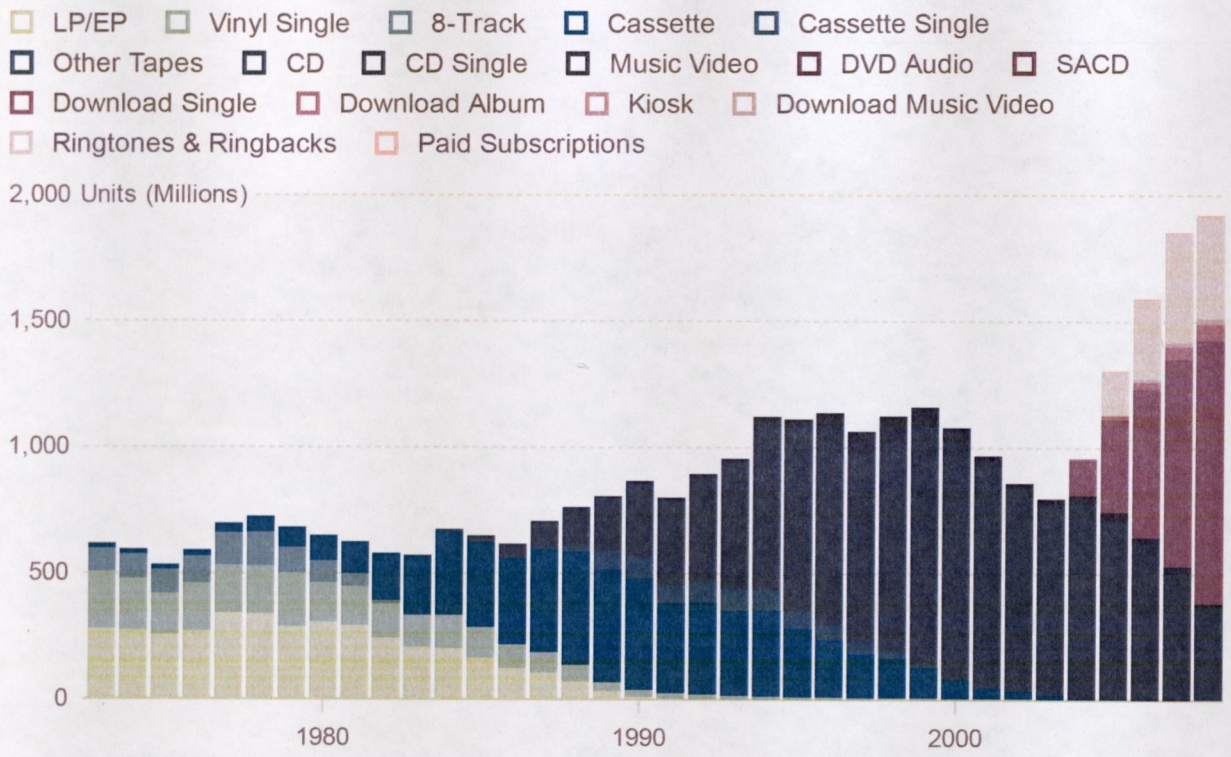
The RIAA provides the most comprehensive data on U.S. recorded music revenues and shipments dating all the way back to 1973. In fact, this is the definitive source of revenue data for the recorded music industry in the United States.

For more in-depth analysis of 2015 data and trends, please see our "News and Notes on 2015 RIAA Shipment and Revenue Statistics. (http://www.riaa.com/reports/riaa-2015-year-end-sales-shipments-data-report-riaa/)" We provide these figures to educate and inform industry discussions, and permission to cite or copy the data is granted as long as proper attribution is given to the Recording Industry Association of America. For further questions, please contact the main RIAA line at 202-775-0101 and ask for Madelyne Adams to help get you the information you need.

U.S. Recorded Music Sales Volumes by Format

RIAA Year-End Revenue and Shipment Reports

Chart Notes



Source: RIAA.

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GRAPHIQ

Total U.S. Recorded Music Sales Volumes by Format | PrettyFamous
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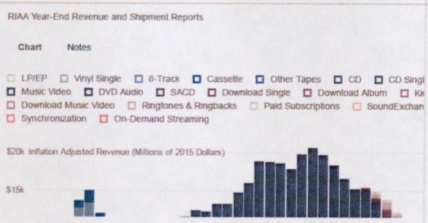
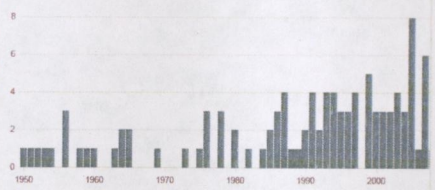
U.S. Recorded Music Sales Volumes by Format



U.S. Recorded Music Revenues by Format



Music Copyright Infringement Cases

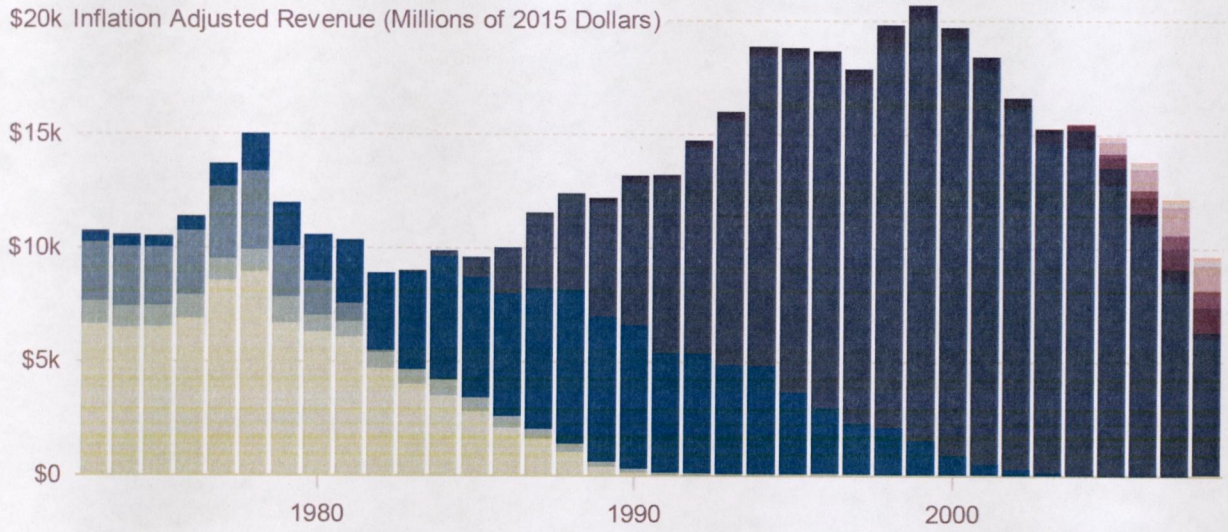
U.S. Recorded Music Revenues by Format | PrettyFamous (https://www.graphiq.com/wlp/2zCGCb5ysKN)

U.S. Recorded Music Revenues by Format

RIAA Year-End Revenue and Shipment Reports

Chart Notes

LP/EP Vinyl Single 8-Track Cassette Other Tapes CD
CD Single Music Video DVD Audio SACD Download Single
Download Album Kiosk Download Music Video Ringtones & Ringbacks
Paid Subscriptions SoundExchange Synchronization On-Demand Streaming



Source: RIAA.

See more details ›

GRAPHIQ

U.S. Recorded Music Revenues by Format | PrettyFamous (https://www.graphiq.com/wlp/7umAJOcO5bT)

(https://www.riaa.com/)

The Recording Industry Association of America® (RIAA) is the trade organization that supports and promotes the creative and financial vitality of the major music companies. Its members comprise the most vibrant record industry in the world, investing in great artists to help them reach their potential and connect to their fans. Nearly 85% of all legitimate recorded music produced and sold in the United States is created, manufactured or distributed by RIAA members.

What We Do (Https://Www.Riaa.Com/What-We-Do/)
Facts & Research (/Reports/)
Gold & Platinum (Https://Www.Riaa.Com/Gold-Platinum/)
News (/News/)
About RIAA (Https://Www.Riaa.Com/About-Riaa/)
Resources & Learning (Https://Www.Riaa.Com/Resources-Learning/)
U.S. Sales Database (Https://Www.Riaa.Com/U-S-Sales-Database/)
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PUBLIC VERSION

MC 50

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Washington, D.C.

In the Matter of:	Docket No. 2011-1
Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services	CRB PSS/Satellite II

STIPULATION OF SOUNDEXCHANGE, INC., SIRIUS XM RADIO INC. AND MUSIC CHOICE REGARDING THE ROYALTY AND MINIMUM FEE PAYABLE FOR THE MAKING OF EPHEMERAL RECORDINGS

WHEREAS SoundExchange, Inc., Sirius XM Radio Inc. and Music Choice (the "Participants") are the only remaining participants in the above-captioned proceeding;

WHEREAS the Copyright Royalty Judges are required in this proceeding to set royalty rates for preexisting subscription services ("PSS") and preexisting satellite digital audio radio services ("SDARS") under Section 112 and 114, including a minimum fee pursuant to Section 112(e)(3) and (4);

WHEREAS the Participants have all submitted proposals for a single royalty rate that would cover both the Section 112 license and the Section 114 license;

WHEREAS the Copyright Royalty Judges have previously adopted combined Section 112/114 royalties with 5% attributable to the Section 112 license and 95% attributable to the Section 114 license (*see* 37 C.F.R. § 380.3 (webcasters), § 380.12 (broadcasters), § 380.22 (noncommercial webcasters), § 382.12 (SDARS), § 383.3 (new subscription services transmitting through video distributors));

WHEREAS such a structure is fully consistent with the Register's decision reviewing the Judges' 2007-2012 SDARS determination, which required a percentage allocation between

Section 112 and Section 114 royalties in the case of a combined royalty (*Review of Copyright Royalty Judges Determination*, 73 Fed. Reg. 9143, 9145 (Feb. 19, 2008));

WHEREAS for PSS, neither SoundExchange nor Music Choice has proposed substantive changes to the existing regulations respecting the minimum fee, which in 37 C.F.R. § 382.2(c) provide for an annual, nonrefundable minimum fee of $100,000 that is creditable toward royalties otherwise due and payable;

WHEREAS for SDARS, SoundExchange has proposed an annual, nonrefundable minimum fee of $100,000 that would be creditable toward Section 112 royalty payments;

IT IS HEREBY STIPULATED AND AGREED by and between the Participants, through undersigned counsel, as follows:

1. In this proceeding, the Judges should set royalty rates for PSS and SDARS that include the royalty payable for the Section 112 license with the royalty payable for the Section 114 license;

2. The royalty payments should be allocated between the Section 112 license and the Section 114 license by substantially the following regulatory language:

> The royalty payable under 17 U.S.C. 112(e) for the making of phonorecords used by the Licensee solely to facilitate transmissions for which it pays royalties as and when provided in this subpart shall be included within, and constitute 5% of, the total royalties payable under 17 U.S.C. 112(e) and 114.

3. For PSS, the minimum fee should be governed by substantially the following regulatory language:

> Each Licensee making digital performances of sound recordings pursuant to 17 U.S.C. 114 and Ephemeral Recordings pursuant to 17 U.S.C. 112(e) shall make an advance payment of $100,000 per year, payable no later

than January 20th of each year. The annual advance payment shall be nonrefundable, but the royalties due and payable for a given year or any month therein under [cross reference to bundled royalty rate] shall be recoupable against the annual advance payment for such year; Provided, however, that any unused annual advance payment for a given year shall not carry over into a subsequent year.

4. For SDARS, the minimum fee should be governed by substantially the following regulatory language:

> Each Licensee making Ephemeral Recordings pursuant to 17 U.S.C. 112(e) shall make an advance payment of $100,000 per year, payable no later than January 20th of each year. The annual advance payment shall be nonrefundable, but the Ephemeral Recordings royalties due and payable for a given year or any month therein under [cross reference to bundled royalty rate and ephemerals allocation] shall be recoupable against the annual advance payment for such year; Provided, however, that any unused annual advance payment for a given year shall not carry over into a subsequent year.

The Participants respectfully request that the Copyright Royalty Judges take notice of this stipulation and adopt the ephemeral recording royalty and minimum fee structures as set forth herein.

Respectfully submitted,

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Counsel for Music Choice

May 25, 2012

CERTIFICATE OF SERVICE

I, Garrett Levin, do hereby certify that copies of the foregoing were sent via electronic mail on the 25th day of May, 2012, to the following:

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Garrett Levin

PUBLIC VERSION

MC 51

Before the
COPYRIGHT OFFICE
LIBRARY OF CONGRESS
Washington, D.C. 20540

In re: Determination of Statutory License Terms and Rates for Certain Digital Subscription Transmissions of Sound Recording	No. 96-5 CARP DSTRA

REPORT OF THE COPYRIGHT ARBITRATION ROYALTY PANEL

11/14/97

cc: DDB
LS
JR

fees in accordance with generally accepted accounting principles. RIAA maintains that these books and records should be retained for at least four years after the period to which they relate. Leibowitz W.D.T. at 6; Tr. 1884 (Leibowitz). The Services' position is that supporting data should be maintained for no more than three years. Terms Submission at 3. See also Copyright Office, Notice and Recordkeeping for Subscription Digital Transmission, Notice of Proposed Rulemaking, 62 Fed. Reg. 34035-34039 (Question for Comment NO.9)(June 24, 1997). The Panel finds that the retention period should be three years. As indicated infra, RIAA itself acknowledges that it should only have the right to audit for three years, and there is a three-year statute of limitations for bringing suit under the Copyright Act. Tr.1992 (Leibowitz); Leibowitz Amended W.D.T. at 7.

193. The Services propose and RIAA agrees that the audit procedure should require timely filing by an interested person of "a notice of intent to audit"; publication of notice in the Federal Register; and that "[o]nly one audit of any service...be allowed with respect to financial records for any given year." Terms Submission at 3; Tr. 1974-75 (McCarthy). So, too, RIAA does not object to the Services' proposal contained at paragraph 300 of its Proposed Findings and Conclusions (even through not originally set forth in the Services' Terms Submission) that RIAA be required to retain an auditor's report for the same period of time that the Services are required to retain documents. See RIAA Reply Findings at paragraph 147. The Panel finds and adopts the foregoing agreements.

194. The Panel also agrees with the Services' position, consistent with the principle of limiting unnecessary expense and disruption, that where a Service can provide an audit already performed in the ordinary course of business by an independent auditor, pursuant to generally accepted auditing standards, such audit and underlying work papers should serve as the audit on behalf of all interested persons unless it can be shown that the auditor did not follow generally accepted auditing standards. This procedure would result in fair opportunity to audit for copyright owners, while

reducing the burden and expense of auditing upon the Services. Terms Submission at 3-4; Tr. 1974-75 (McCarthy).

195. The Services propose that RIAA and other interested parties pay the expenses of an audit unless there is a "judicial determination" or an agreement by the affected Service that there was an underpayment of royalties of 5 percent or more. Services PROPOSED FINDINGS & CONCLUSIONS at ¶ 166. Leibowitz W.D.T. at 6-7; Tr. 1884-85 (Leibowitz). However, RIAA contends and the Panel concurs with RIAA that the Collective should not have the burden of filing a lawsuit to have a Service reimburse the audit expenses where an independent auditor concludes that there has been such an underpayment. In that situation, the burden should fall on the Service to justify its payment. Indeed, RIAA's audit proposal is modeled after the Services' own affiliation agreements.

CONCLUSIONS

196. On the basis of the written record constituting the testimony and evidence in this proceeding, prior decisions of the Copyright Royalty Tribunal, prior copyright arbitration panel determinations and rulings by the Librarian of Congress under section 801(c), 17 U.S.C. §801(c), and the Findings of Fact set forth above, the Panel concludes that:

I. COMPLIANCE WITH THE STATUTORY OBJECTIVES LEADS TO A ROYALTY RATE OF 5%

197. DCR, DMX and Muzak each comply with the factors set forth in the 1995 Act, 17 U.S.C. §114 (d)(2), and thus qualify for a compulsory license to perform sound recordings.

198. The Panel has considered the various objectives set forth in the Copyright Act in going about its task of setting a "reasonable" rate and terms. As to each objective, it concludes as follows:

MC 52-60
FILED UNDER SEAL